# REAUTHORIZATION OF FARMERS HOME ADMINISTRATION LOAN LEVELS FOR FISCAL YEARS 1983, 1984, AND 1985

## HEARINGS

BEFORE THE

## SUBCOMMITTEE ON AGRICULTURAL CREDIT AND RURAL ELECTRIFICATION

OF THE

## COMMITTEE ON AGRICULTURE, NUTRITION, AND FORESTRY

## UNITED STATES SENATE

NINETY-SEVENTH CONGRESS

SECOND SESSION

ON

## S. 2314

AN ACT TO AMEND THE CONSOLIDATED FARM AND RURAL DEVELOPMENT ACT

APRIL 15 AND 21, 1982

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# REAUTHORIZATION OF FARMERS HOME ADMINISTRATION LOAN LEVELS FOR FISCAL YEARS 1983, 1984, AND 1985

THURSDAY, APRIL 15, 1982

U.S. SENATE,
SUBCOMMITTEE ON AGRICULTURAL CREDIT AND
RURAL ELECTRIFICATION OF THE
COMMITTEE ON AGRICULTURE, NUTRITION, AND FORESTRY,
*Washington, D.C.*

The subcommittee met, pursuant to notice, at 2:07 p.m., in room 324, Dirksen Senate Office Building, Hon. Paula Hawkins (chairman of the subcommittee) presiding.

Present: Senators Hawkins, Jepsen, and Zorinsky.

## STATEMENT OF HON. PAULA HAWKINS, A U.S. SENATOR FROM FLORIDA

Senator HAWKINS. Today, the Subcommittee on Agricultural Credit and Rural Electrification will conduct a hearing on reauthorizing the major rural loan programs administered by the Farmers Home Administration for fiscal years 1983, 1984, and 1985.

The Farmers Home Administration has been serving the rural communities of America since 1918. Its programs have long been important to the economic stability of America's rural regions. As the lender of last resort, the Farmers Home Administration plays its most important role by providing operating and ownership loans to American farmers unable to obtain credit elsewhere. Over the years, the role of Farmers Home has been expanded by Congress to include crop disaster relief loans, water and sewer facility loans, and loans for community and industrial development. Finally, since 1978, the Farmers Home Administration has made economic emergency loans to farmers in need because of economic circumstances beyond their control.

In fiscal year 1981, the Farmers Home Administration made 210,339 farmer program loans totaling over $8 billion. This was 11 percent of the total agricultural credit extended to farmers. Without a doubt, the activities of the Farmers Home Administration are of the utmost importance to the stability and productivity of America's farm community. But today, the Farmers Home Administration faces a difficult challenge.

Farmer net income has declined from $27.4 billion in 1979 to $19 billion in 1981. After adjusting for inflation, this amounts to a 45-percent drop in real income. Projections made by the USDA, the Farm Credit Administration, and private sector economists indi-

cate that no real improvement in net income should be expected in 1982. These grim statistics ironically result from the hard work of America's farmers and the natural abundance of our land. Food production in 1981 reached an all-time high and unsheathed a two-edged sword, cutting into inflation but slicing into farm income at the same time. During these difficult times, the Congress must define the role Farmers Home should play in financing agriculture. In making this definition, we shall look at the overall farm credit picture which, despite low income, in many ways is strong. Soaring land values have driven the assets of established farmers up more rapidly than debts. In 1971, farmer's equity—the difference between total assets and total debts—was only $272 billion. In 1981, equity rose to $912 billion. Since equity represents the collateral base for lenders, it is clear that farmers, as a whole, should not have difficulty acquiring credit although interest rates are higher than normal.

Of course, averages can be misleading. If a millionaire and pauper are in a room together, the average salary for people in the room is $500,000. Similarly, farmers who come to the Farmers Home Administration are not typical farmers. They usually have not been farmers long, and unlike the average farmer, they have more debts than they have equity. This means that lending to such farmers involves more risks than the banking industry would voluntarily take. If 2 or 3 percent of a bank's loans are delinquent, then the situation is considered serious. In January, over 50 percent of the loans made by Farmers Home were delinquent. It could be higher next January.

Delinquent loans, even if they are eventually paid in full, cost the taxpayers money and drive up the deficit. While the Government waits for payments expected, the Treasury must raise new funds to cover the shortfall. Clearly, a reasoned and practical approach is required if we are to protect farmers in difficulty and the taxpayers at the same time.

One way we can protect taxpayers is to require borrowers to purchase crop insurance and to use more aggressively hedging opportunities available in futures or options markets. That way, crop failures or low prices will not destroy the ability to pay.

Another area that greatly concerns me is the fact that the Farmers Home Administration has experienced great difficulty in installing a computerized management information system. The agency has been trying to put a comprehensive computer management system on line since 1975. In the coming weeks, I intend to take a very close look at ways to expeditiously get such a system in place.

In addition, our office has been investigating any number of new ideas, including but not limited to: (1) requiring variable interest rates for loans and/or graduated interest rates, depending on ability to pay; (2) requiring a recapture of the subsidy in the limited resource loan program when borrowers either graduate from Farmers Home to private lending or have sold the land and realized a profit; or (3) requiring borrowers to purchase Federal crop insurance in order to be eligible for disaster assistance loans; (4) establishing a quasi-governmental rural development bank similar to the banks established in the Farm Credit Administration.

With these thoughts in mind, our subcommittee will take a close look at the proposals the administration has made for reauthorizing the Farmers Home Administration programs that fall under our jurisdiction.

At this time, I would ask Senator Zorinsky if he has a statement.

Senator ZORINSKY. I have no statement.

Senator HAWKINS. Senator Jepsen?

## STATEMENT OF HON. ROGER W. JEPSEN, A U.S. SENATOR FROM IOWA

Senator JEPSEN. Thank you, Madam Chairman. You are to be commended for calling these hearings on legislation to reauthorize the loan ceilings for Farmers Home Administration farm and rural development credit programs. These hearings, however, I would suggest, go beyond the question of reauthorizing a program or a series of programs, as important as this reauthorization is.

These hearings involve more than credit, as critical as it is today. These hearings go beyond the need for fiscal restraint, as vital as it is to balance the budget and get rid of deficits.

What this hearing is all about are people and whether we in Washington are listening to them. Survival is the name of the game—survival of farming as a way of life.

The depressed farm economy is forcing our farmers to revise their visions of the future. They do not know whether they will make it. They do not know what they will do if they do not make it.

An Iowa farmer recently told a Wall Street Journal reporter: "I do not want to be an old man scrubbing floors. I do not want my wife to have to, either."

Farmers are turning into pessimists when, by nature, they are and have been optimists. Farmers do not want handouts, but they expect a Government which has helped create their problems to show more understanding toward their plight. They do not expect their Government to reject out of hand every proposal advanced to help them over these bad times. When farmers are suffering through their third consecutive year of low income and low prices, someone must listen. When interest rates are so high that farmers can no longer afford the purchases which ripple into a sound economic foundation for rural America, someone must listen. When the market prices for commodities are less than the costs of production, someone must listen.

If the administration does not act, then the Congress will be forced to. The administration should not be pitted against the Congress, nor Republican against Democrat, when it comes to the well-being of our farmers.

According to a comment contained in the U.S. Department of Agriculture's handbook, "A Brief History of the Farmers Home Administration;" economic emergency loans are designed to help farmers overcome economic hardships caused by credit scarcity of cost/price squeeze beyond their control. I would suggest that this is reason enough to implement—with appropriate restrictions to prevent abuses—the $600 million economic emergency loan program called for in the 1981 Farm Act.

It is not good enough to argue that we have to turn over Federal lending programs to the commercial sector. It is a laudable goal. It is the direction that we ultimately must go; but it must be done gradually and this is not the time. I do not feel it would be out of order—for these are not ordinary times—for the administration to revise its regulations so that farm loans can be rescheduled at the original rate of interest agreed to at the time the loan was obligated.

I feel, as others do on the Senate Agriculture Committee, that this change in the regulations will be consistent with the Government's original commitment to the borrower, protect the Government's investment, and prevent unnecessary foreclosures and liquidations of assets.

I believe every effort should be made to help those farmers who have made reasonable and honest attempts to repay their loans but have been unable to do so because they are cash-strapped as a result of low commodity prices. These are two areas, Madam Chairman, in which the administration can act on its own. It would make unnecessary legislation such as that introduced by some of us on the Senate Agriculture Committee. Taking these steps would be, as Senator Boren has stated it, "both compassionate and prudent."

The consensus is that a majority of farmers who have adhered to a conservative financial program for the past few years probably will have or will receive sufficient funds to carry them through the 1982 crop season. That is not to say they will not be heavily in debt, because they will be; but there is also a consensus that if prices continue as they have, if farmers are unable to show a profit this year, they face big trouble. To be blunt, they will go under. The unspoken question out in Iowa and elsewhere across the Farm Belt is: Who will be the first?

So the basic question I have of the administration witnesses today is: Has the administration any plans—any contingency plans—to deal with this problem, to deal with a situation in which farmers again will show no profit this year, to deal with a situation in which the debt problem worsens?

I thank you, Madam Chairman.

Senator HAWKINS. Thank you.

We have with us today, as our first panel, Frank Naylor, who is the Under Secretary for Small Community and Rural Development, and his colleague, Charles W. Shuman, who is the Administrator of the Farmers Home Administration.

Mr. Naylor, do you have a statement?

**STATEMENT OF HON. FRANK NAYLOR, UNDER SECRETARY FOR SMALL COMMUNITY AND RURAL DEVELOPMENT, U.S. DEPARTMENT OF AGRICULTURE, ACCOMPANIED BY HON. CHARLES W. SHUMAN, ADMINISTRATOR, FARMERS HOME ADMINISTRATION**

Mr. NAYLOR. Madam Chairman, it is a pleasure for us to be with you today. We are very appreciative of your calling these hearings and giving us a chance to review what progress and actions we are taking in working with the farm community and to review with you the administration's proposal for reauthorization of the Farmers Home Administration authority.

I have just a few brief comments, if I may, Madam Chairman, and then Mr. Shuman, the Administrator of Farmers Home Administration, does have a short, prepared statement to share with you.

About a year ago, Madam Chairman, when we appeared before your committee during a time of confirmation, we indicated at that time that our objective was to return to what we felt were some of the basic tenets of the Farmers Home Administration, and that was to meet some rather fundamental needs of the agricultural community and of the rural community as a whole. I think we have succeeded in doing that. We have substantially strengthened the activity in our Farmers Home and agricultural lending, and in fact this administration in 1982 increased by 50 percent the amount of operating loan funds which would be made available for this coming year, anticipating that there would be a requirement for additional production lending. We have continued to make available our emergency disaster lending program, because we recognize the need and role it serves while the crop insurance program is being brought on line and developed into a successful program to meet the disaster requirements and needs of American agriculture.

We propose in 1983 again to increase the amount of funds available for agricultural lending and are prepared to meet our commitment for production lending for American agriculture where it is necessary for us to fill that role and void left by the commercial sector or Farm Credit System, and responding to those individuals who, through no fault of their own, temporarily have been unable to get credit in normal sources and must look to the Farmers Home Administration for assistance.

I, as well as Secretary Block and those of us in the Administration feel very strongly that the long-term picture for agriculture is strong. Just a few weeks ago, the total value of farms and farm assets of all types passed the $1.2 trillion mark, while total debt outstanding has not yet, but will this year sometime pass $200 billion. Half of the American farmers have no debt at all, of any kind, and have prudently managed their operations and have done so successfully. This is not to cast any lightness on the problems that are faced by many producers today. We do have many producers, particularly in the South and in some spotty areas of other parts of the country who are experiencing their second, and in some cases, their third year of serious cash flow problems. And I believe we have a commitment and an obligation to service those producers and provide them with the support that we have been directed through the Congress to do, and we have done that successfully.

We are almost through, Madam Chairman, our lending season. This is the predominant period in which farm loans are made to the farming community. I think we have succeeded in responding to the needs, both through a unique step that I have never seen before in Government, in which Secretary Block called together the commercial lending sector, the farm credit system, and the Department of Agriculture, to work on a coordinated basis to meet the production lending needs of American farmers. I think we have succeeded in that. I regret that we have lost some farms, and that, perhaps, there was no way to avoid. But we have taken extraordi-

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nary measures to do everything within our power to keep every producer who had any opportunity at all of success to continue in operation, including deferments, reamortization, reschedules, and subordinations for the commercial sector. I think we have been successful in limiting the number of losses of farms to quite a low number, and we will have a substantial opportunity for the farming community to work together through this economic recovery period.

I think we are on the right path. I look forward to your review of the request and proposal by the administration to reauthorize, if necessary, authorities for the administration to continue on this path of support in the future with the reauthorization of the Farmers Home Administration authorization for 1982.

Senator HAWKINS. Mr. Shuman.

Mr. SHUMAN. Madam Chairman and members of the committee, I appreciate the opportunity to discuss policies and actions of the Farmers Home Administration in serving farmers and rural communities through the programs of FmHA.

As of today, as Secretary Naylor indicated, we are in the advanced stage of an extraordinary effort to meet the needs of the Farmers Home Administration farmer borrowers in a year of much difficulty for various sectors of agriculture, in various parts of the country.

As the winter and spring season of farm production lending nears its conclusion, we still have a substantial amount of operating loan funds available. We are confident that the resources exist, in Farmers Home Administration and with other lenders, to meet the needs of farmers who have the capability to continue in farming and eventually stabilize their financial situation.

We have made a special effort to subordinate liens to other lenders so that they can help FmHA borrowers not eligible for our credit this year. Subordinations have progressed at about double the rate of recent years, and we are gratified that other lenders have responded so well in accepting our subordinations.

Delinquency in farmer programs are still higher than normal, as you indicated, but have been paid down substantially from the high point on which the year began. The interest rate for production loans has moved downward since the first of the year, and prospects are that this trend will continue as benefits of the President's economic recovery program take greater effect as time progresses.

In looking ahead to the next fiscal year, the bill S. 2314, which you have under consideration, is one that we recommend as making ample provision to provide a last-resort source of credit to family farmers, and support the needs of rural communities for essential public facilities.

The bill would continue FmHA's fundamental farm real estate and production loan programs at the $2.2 billion level; in fact, it raises the production loan authorization, as Secretary Naylor indicated, from $1.375 billion to $1.51 billion in 1983. It proposes a firm ceiling of $1.54 billion for the disaster emergency authorization, which will be sufficient unless there are major unforeseen needs to be dealt with by supplemental authority. It provides for loan authorizations of $300 million for water and waste disposal project loans, and $130 million of loans to finance other community facili-

ties in truly rural communities that can find no other source of assistance.

The bill omits any request for authorization to continue the business/industrial loan guarantee program. Given the present impetus of rural growth and resources available from the private sector to business and industry in rural areas, resources of Farmers Home Administration we feel will be better concentrated on those areas of agriculture and community needs where no alternative to our service exists.

The bill would delete from the Consolidated Farm and Rural Development Act the authority of section 310D to make nonemergency farm loans at deeply subsidized interest rates to farmers operating in a situation of low income. Aside from budget considerations, our experience shows that, with adequate loan supervision assistance from Farmers Home Administration, farmers of limited resources can develop sounder operations by working from the beginning on the basis of unsubsidized credit.

Madam Chairman, with those brief summarizing remarks, I will be glad to answer any questions that you and the committee may have.

Thank you.

Senator HAWKINS. Thank you, gentlemen, for coming.

During my review of the Farmers Home Administration, I became concerned that we find ways of protecting taxpayers' money when it is borrowed by high-risk Farmers Home borrowers. Do you have any suggestions as to how steps might be taken to protect Farmers Home loans against loss due to natural disasters or the extremely low farm prices that we are having today?

Mr. NAYLOR. Madam, as I think you are aware, the administration has supported and is pursuing the implementation of a Federal crop insurance program. We had some major learning lessons to overcome this year, and we are in the process of learning from that and taking the bugs out of that program, which is experimental in nature and is now suddenly grown to one of major national importance and value. It is our belief that the underlying answer to natural disasters and disaster problems for the farming community should lie in this insurance approach, that that is a more realistic way of treating a casualty loss. If a businessman's business burns down, he has it insured; if it is the corner store, or his inventory, he is insured. He does not go out and borrow money to restart again.

We have typically expected our farmers, on the other hand, to borrow to replace their losses, and that only makes their indebtedness situation worse and makes their recovery more difficult. It is our belief that the crop insurance program offers the best long-term solution to that underlying problem of dealing with disasters, which most typically are the major impacting factors and causes heavy debt loads to develop. We think it will probably take another year, perhaps not more than 2—to bring that program fully on line and fully supportive of the entire agricultural community. We feel this administration is committed to doing that.

Senator HAWKINS. What about the agricultural options or the use of the futures markets?

Mr. NAYLOR. Mr. Shuman is our expert in that area. I will turn to him, Madam Chairman, if I may.

Mr. SHUMAN. I think, Senator, what you are probably referring to is the need for agriculture and farmers to pay more attention to their marketing plans and marketing techniques. The futures market is a way in which, if used properly, many sophisticated operators can reduce risk. The whole marketing concept is something that I would agree needs to be looked at more thoroughly and more completely by all of us in agriculture.

Senator HAWKINS. Early in the year, there was a great deal of red flag waving over the way Farmers Home was treating delinquent loans. We have heard Senators talk about that, and it is in the record. Several Members of Congress proposed a moratorium on loan repayment because of the financial difficulties farmers are experiencing. Would you explain your view of this situation and what actually transpired and what steps Farmers Home has taken to deal with its high rate of delinquency?

Mr. SHUMAN. The delinquency rate, as you indicated, that Farmers Home Administration is experiencing is of great concern. As any lender, we do not like to see delinquencies up; we do not like to see them continue high. But of even greater concern to me is the cause for those delinquencies. In an effort to more adequately service those delinquent accounts, Farmers Home Administration, about a year ago undertook, I would say, a slight change in direction. We started emphasizing more supervising and servicing of all our accounts, including the delinquent accounts, in an effort to insure success on the part of our farm borrowers. That supervisory and servicing activity has not been as fruitful as far as reducing delinquencies as some people had hoped, but we do think that the long range effect of that will be productive.

In addition to that change in direction, the Department, people in the agency, and myself, did continually monitor the financial situation of farmers and especially Farmers Home Administration borrowers, and as a result of that monitoring, the Secretary of Agriculture in January called the meeting that Secretary Naylor referred to just recently, and asked for the cooperation of all lenders that supply credit for agriculture in finding ways to stay with farmers during this rather tough time. And the Secretary directed the Farmers Home Administration to take certain actions, which we implemented early in February. We feel that those steps, our emphasis on supervising and servicing, on a one-on-one basis, and our willingness to continue with our present borrowers from year to year, does and will continue to make sure that adequate credit is provided to rural America.

Mr. NAYLOR. Madam Chairman, may I add just a comment to that, with your permission?

Senator HAWKINS. Surely, Mr. Naylor.

Mr. NAYLOR. We have looked at this situation very closely, and I am well aware that there have been a number of proposals for various forums and moratoriums or set-asides as far as payments are concerned. Under the present law, we have a great deal of discretionary authority to do those sorts of things which I have mentioned earlier. One thing that I believe the moratorium concept significantly overlooks is the fact that each and every producer, like

any other human being's situation is different. They need to be treated with compassion, and each individual case needs to be treated slightly differently.

There is no one solution, which we tend to do too often at the level of Federal Government that will solve everybody's problems. A moratorium and a general forum will not solve the problems of the American farmer any more than an American farmer or any other businessman can borrow his way into prosperity. The real need is stronger prices, better exports and lower interest rates, all of which are being significantly addressed by this administration.

I think we have used the authorities available to us, and contrary to many shrill and very loud reports in papers and statements by various figures around the country, the truth is that we have been able to maintain a very, very low level of loss of farmers, and we have been able to refinance and provide the financing necessary for operations in this coming year.

I would hate to see us get in a position where I would have to answer to the other 85 percent of the American farmers who do not borrow from Farmers Home, but who borrow from commercial sources or borrow from the farm credit system and then are expected to pay their loans on time and do so; and for that matter, the two-thirds to three-quarters of our farmers who, despite their conditions, have had either profitable years or have the capacity to pay their loans on time.

I do not think the farming community would look favorably on us if we granted that type of general moratorium and exempted a very limited number of people from paying that would not even in that case really be helpful to them. They need individual attention, individual supervision, they need prudent use of the authorities that are available to us, but they need it on a case-by-case basis.

Senator HAWKINS. Senator Zorinsky.

Senator ZORINSKY. Thank you, Madam Chairman.

Mr. Naylor, I notice you made a good case in point for a farmer to be able to insure himself, as any other business, against problems or deficiencies. Where would you go to get insurance against the volatility of a commodity price that is directly, proportionately related to Soviet intervention in Afghanistan or our administration's neglect in not wanting to talk to the Soviet Union about a 5-year farm grain agreement. The Secretary of Agriculture sat right in that chair and said it is to our best interest, to the farmer's best interest, to have a 5-year farm agreement, but it really did not make that much difference, because if the Soviets call this afternoon, we will sell them grain. To me, that implies, and to the farmers of America, that it is OK to sell the Soviets grain, but it is not OK to talk to the Soviets about selling grain.

Where do they go to alleviate that condition? The point I am trying to make is unlike many other industries and businesses, agriculture's problems in many respects are unique to that particular industry, especially if the Federal Government gets in and screws it all up for them.

Mr. Naylor, you have made several public statements indicating that you are very optimistic about the soundness of the farm economy, and you base these statements on the debt-equity ratio for farm operations. Hasn't the debt-to-equity ratio been relatively fa-

vorable for farmers because of the paper value of farmland that has increased each year in the recent past, and what would be the effect on lenders and farmers if land values begin to decrease, as I believe they already have. People are finding out land is only worth as much as somebody will pay for it. And do you or do you not agree that the high percentage of earnings farmers must set aside for interest payments indicate an unhealthy farm economy?

Mr. NAYLOR. Senator, I think there is no question that there are a number of producers, particularly those who have been required to borrow a substantial amount of money in recent years, that are experiencing short-term cash flow problems, some quite serious, as a result of a combination of factors. For example, in the South, it has been a combination of several years of poor crop conditions, combined with high interest rates and with the abundant crop this year and low commodity prices. I certainly recognize your concern, and we are monitoring very closely the question of farmland values and the values of total assets. I think we have observed some flattening, but I would hasten to say that I would not attribute the current land values to what an individual farm sale in one particular situation under those kinds of conditions might create, as opposed to a normal transaction in the real estate sense of the year. Also, I think this year is a little unusual, and we need to factor that into our thoughts, in the sense that many farmers, because of the cash flow conditions, are cutting back on their individual operations and are not aggressively expanding; they are taking a wait-and-see look, to see how the commodity stocks fall off and how the prices strengthen. So there has not been the aggressive competition for cash rent and for new purchases and expansion of lands.

I think as we begin to see the President's economic recovery program take effect, and we begin to see interest rates continue to decline, and as we begin to see some strengthening in prices as a coordinated export program by this administration begins to bring fruit, you will see strengthening again, and you will see the farm picture improve markedly.

Senator ZORINSKY. What gives way to the optimism on the lower interest rates as we approach the third and fourth quarters? Does it have anything to do with, hopefully, a balanced budget, or is this something that has something to do with planting more acres?

Mr. NAYLOR. I think the optimism has to do with the overall interest rate picture itself and the direction the economy is heading. I think we are going to begin to see a sustained economic recovery toward the end of the second quarter, the beginning of the third quarter. I think we have bottomed out, as Secretary Regan has indicated, as well as Secretary Block has on several occasions. Interest rates, particularly short-term rates, should be lower than what they are now. If you use traditional economic examples, they should be several percentage points lower than what they are now. I think we will continue and can look forward to a continued downward trend in interest rates and some improvement in that picture, and it will certainly have a substantial impact on the farming economy, as we are all aware of the serious nature and the magnitude of the effect that interest rates have on our agricultural operations.

Senator ZORINSKY. I certainly hope that you are right, and I will do everything I can to make that prediction come about, in cooperation with the administration, hopefully toward eliminating the deficit in our budget. But I have to point out, in all honesty, that those people who live by the crystal ball end up eating glass sometimes.

Mr. NAYLOR. I am well aware of that, Senator, and I long ago learned that economists have a wide range of discretion in their predictions. They often fall short, and it is not a prudent man who makes hard predictions on those kinds of changes. I think we have seen genuine progress in the inflation rate. I think we are beginning to see progress on the monetary scene, and that we can look forward to a sustained economic recovery beginning to take effect, shortly.

Senator ZORINSKY. Well, I have seen a great deal of progress in unemployment, and I have seen a great deal of progress in increased deficit numbers in our budget, and I hope we can reverse those trends, also.

Mr. Shuman, in view of the record low farm income and high interest rates and high production costs, do you feel that farmers are facing an economic emergency, and if so, do you anticipate making any economic emergency loans available this spring?

Mr. SHUMAN. As far as the economic emergency loan program is concerned, Secretary Block has indicated the specific criteria that he would like to have us monitor, and we are monitoring those criteria. The Secretary has said that if those criteria deteriorate enough, he will make designations on a State-by-State basis. We are also writing some changes in our economic emergency loan procedures so that an economic emergency loan applicant would first have to be found ineligible for our more conventional programs.

As far as the general question about the conditions facing the farmers is concerned, things are difficult for many producers of agricultural commodities. Farm prices are lower than many people anticipated. Interest rates have not come down as fast as many people thought. And even though we have made some substantial steps toward dealing with the inflationary problems, production costs are still high.

So, generally speaking, there are problems as far as income is concerned, and the Secretary has made some indications as to the criteria he will be utilizing in releasing or designating areas available for economic emergency loans.

Senator ZORINSKY. Then, you do anticipate making economic emergency loans this spring?

Mr. SHUMAN. Secretary Block has not yet made any designations. That would be at his discretion.

Senator ZORINSKY. Then, he has authorized the evaluation as to eligibility for the loans, but he has not made the determination that, in effect, if the criteria are met, that the loans should be made?

Mr. SHUMAN. He has indicated to us the criteria that he wants us to monitor, which we are monitoring.

Mr. NAYLOR. Senator, under the regular emergency disaster program, there is a wide range of eligibility under that, both from the current year and from prior years. There are no restrictions on

that program or the availability of funds this year, and we are using it extensively. We have an agreement within the administration to provide whatever funds are necessary under that program, and we have been making substantial amounts available. We have been making extensive use of the operating loan program and our subordination and guarantee authorities in cooperation with the commercial sector for some special cases. We still have over $600 million left in our operating loan program, which is unusual for this time of the year, but it is indicative, I think, of our provision for a 50-percent increase in funds over prior year levels. Simply stated, we have adequate funds to meet the borrowing requirements of our producers at this time, and we expect that we will complete the lending year within our available resources that we have right now.

Senator ZORINSKY. Thank you.

Mr. Shuman, it is my understanding that Nebraska has one of the highest percentages of delinquent Farmers Home Administration farm loans of States in the Midwest. I am very concerned about the prospect of farm foreclosures for some of these borrowers. At your confirmation hearing, I was particularly pleased to hear your statement about foreclosures. You said, and I quote:

> Foreclosure is any kind of liquidation, whether it is voluntary of involuntary liquidation, of a man's business, his farm, and that is the last thing we want to do. That means that everybody has failed and we do not want to do that.

Is it true that the Farmers Home Administration will foreclose, using the definition of foreclosure, on more farmers this year than any other year in the history of the agency?

Mr. SHUMAN. I do not know the entire history of the agency, but I can say that our foreclosure rate this year is very low, and somewhat higher than last year.

Senator ZORINSKY. Very often people prior to going broke or being foreclosed on or being delinquent are knowledgeable enough in their own business and in their own right to see the handwriting on the wall too, and one of the alternatives obviously is a farm sale, in advance of that happening. I am a personal acquaintance of an editor of a newspaper in Syracuse, Nebr., and as a sideline to printing a newspaper, they also do outside printing, and they also print farm sale bulletins that they put on the walls everywhere to notify people of a sale. And he has indicated he has printed more farm sale bulletins within the last 2 months than he has printed in the last 6 years. I think this may be of concern and may be an ominous sign as to the prelude to the time that you become involved in some of those things.

Mr. NAYLOR. Senator, I appreciate that concern, and we share it, too. We are monitoring those same types of numbers ourselves, not only our own, but other situations. All lenders have a responsibility within a community, to work with farming, agriculture and the rural communities, to maintain a viable and productive agricultural economy. We monitor not only those losses of farms that have resulted from our inability after exhausting every authority we have, every ability we have, to help the producer and are unable to do so. We also monitor those that take the action you are talking about, voluntarily deciding that it is better for them to look for

some other business opportunity or to be foreclosed upon. The numbers are still very low, not just about Farmers Home, but all sources—are not substantially higher than a year ago. There are hot spots. There are locales where, for whatever reason, seem to be particularly in difficulty at the moment. We have identified several within Farmers Home, for example, around the Lubbock area in Texas, around the delta area in Mississippi, south Georgia, a few places in the Carolinas, a couple places in your State, where there seem to be more than you would expect. We are trying to do everything we can to help those particular areas and go an extra mile with them.

Senator ZORINSKY. Thank you.

Madam Chairman, I assume we are on the 10-minute rule, and I have some more questions, but I will defer at this point to Senator Jepsen.

Senator HAWKINS. Senator Jepsen.

Senator JEPSEN. Thank you, Madam Chairman.

On a positive side for a moment, I sat in another hearing this morning and heard some say that there was no compassion in the Department of Agriculture, that they did not understand and were not sympathetic to the farmers' problems. I do want to go on record, by way of some questions to help clear this matter up, especially with the Farmers Home Administration.

Is it accurate to say that over $500 million more this year was made available through Farmers Home for operational loans than was the year previous?

Mr. NAYLOR. That is correct, Senator, it was.

Senator JEPSEN. Is it also accurate to say that $135 million additional has been requested next year for farm operational loans by the Department?

Mr. NAYLOR. Yes, Senator, that is correct.

Senator JEPSEN. I see a great deal of compassion and awareness of what the problems are with that type of money being put, when in most areas, there has been a dramatic reduction. Some of those, I do not agree with. But certainly, in this area, to give credit where credit is due, it does seem to me that if there is any problem here, it has been one of communication. Reports from around the country, from various congressional offices, would indicate that there has been some possibly uneven implementation of Farmers Home directives and of its discretionary authority to defer consolidating, rescheduling and reamortizing loans. There are reports from some Farmers Home borrowers that circumstances beyond their control and unduly quick action by Farmers Home personnel are forcing them to liquidate their farming operations voluntarily, as you indicated, in order to avoid foreclosure by Farmers Home I also hear more frequently that there is no money or loans available—primarily by critics of the administration, I might add. That is just not so, is it?

Mr. NAYLOR. No, Senator. There is no shortage of funds. We have adequate funds available. Mr. Shuman has provided additional staff where necessary because of disaster lending. As you know, we always have an extremely busy period because every farmer tries to get his production loan application in within a 2- or 3-month period as he is planning his new year. It would be nice if we could

spread those out over the year, but that is not what happens. But nevertheless, I think Mr. Shuman has done a very fine job of getting resources into place and to carry out that assignment. I would like Mr. Shuman, if he may, Senator, to comment on the direction and his feeling with regard to specific handling of loans.

Mr. SHUMAN. As the Secretary said, we do have adequate loan funds available. The reason for those funds being so adequate at the present time is twofold: first, the $500 million increase that was available to us in 1982 and second, the excellent reception that the conventional lenders have given to our subordination authorities. So, for those two reasons, we are finding that we do have plenty of funds available. If you do have locations where someone has made this statement, we would be more than happy to dig into that situation and find where the miscommunication is, because we do have adequate funds.

Senator ZORINSKY. Would the Senator yield for just a second, on this subject?

Senator JEPSEN. Certainly.

Senator ZORINSKY. Are you having any problems, with regard to being able to have enough manpower to service these loans, or have you got a personnel shortage, because this has happened in the past because people are saying, "Gee, it takes a long time." Is there any relationship?

Mr. SHUMAN. As far as the time it takes to process a loan, I remember very distinctly here for my confirmation hearing when Senator Andrews asked me—or pretty near mandated—that if I wanted to be a successful Farmers Home Administration Administrator, I should find ways to shorten the time it takes to process a loan. We are working in that regard. I would like to have Senator Andrews think that I was a successful Farmers Home Administration Administrator. I do not know whether I will be able to get that job done or not. We are trying to find ways in which we will shorten the time it takes to process loans.

As far as people resources are concerned, I do not think that there has ever been a time in Farmers Home Administration's history when we could say that we had the absolute number of people that it would take to do everything perfectly. As a result, as managers, then, what we have to do is take the resources available to us and put them where they are needed the most, and that is the effort and the tactic we are taking. We have said that our No. 1 priority right now—and we are about to finish that priority is making credit available for operating purposes in our farm loan areas, and during this period of time, while that is the most critical need of the rural areas, that is where we are putting the emphasis and our people resources.

Senator ZORINSKY. Thank you.

Mr. NAYLOR. Senator, if I may make a comment on that. As we did with the operating loans, I think it is particularly unique in recognition of the problems Farmers Home has faced in the last 2 years and the importance of operating that program properly. Unlike most agencies in this city that have faced personnel reductions, along with budget reductions as part of that effort to withdraw some of the Federal activity, we have not had a personnel reduction in Farmers Home Administration on our permanent em-

ployees. We continue to have the authority in our disaster loan program to bring on what emergency employees are necessary to deal with our problems. I think that is significant, and it has helped us do a better job. I would have to say to you that I can remember when I was in Charlie's position a few years back, and every spring, we would go through this crunch of spring lending. We would get backed up on our loans, because all farmers, instead of getting them in on a spread-out basis wanted to try and process their loans at one time. To Mr. Shuman's credit, we have seen significant progress this year. A year ago, the new administration, the major problem was the breakdown of a computer in St. Louis. No checks were being delivered at all to farmers until mid-April. We were delivering checks to farmers by February 1 this year. That is not perfect, but it is a significant change.

Senator ZORINSKY. I am sure all of us will agree that all the money in the world will not solve a problem if you do not have the personnel to process and administer the money.

Mr. NAYLOR. In further response to some of these criticisms, I further recall Secretary Block in late January said that while the farm sector faces difficulties for the moment, the USDA's—and I quote him here—"objective is to keep farmers in business." That is not displaying a lack of compassion for the working farmer, as far as I am concerned. He indicated that Farmers Home will use its discretionary authority to assist farm borrowers who are experiencing difficulties on a case-by-case basis. Question: Do you have any estimate on the number of farmers that you have kept in business as a result of this policy?

Mr. SHUMAN. I will supply that for the record, Senator—is it is available—but I can give to you an up-to-date number of the number of loans that we have made so far this year. I think a substantial number of those borrowers were kept in business because of this compassion.

Senator HAWKINS. I have some figures here. Would you recognize them, if I were to insert them, to be accurate? So far this fiscal year, through March, 15,535 farmers have been accommodated through subordination of Farmers Home liens as compared to 25,980 given operating and ownership loans.

Mr. SHUMAN. That is one area in which we have been active, but the total number of loans that we have made this year would be much higher than that, and I will get that for the record.

Senator HAWKINS. Thank you. We needed that. We could not get it.

[The following response was received by the committee:]

Through March 31, 1982 we had obligated 47,732 production type loans totaling $2,094,203,170; 23,048 operating loans for $657,322,340 and 24,684 emergency loans for $1,336,880,830.

Senator JEPSEN. Mr. Shuman, during House hearings, you said that Farmers Home delinquencies are about 10 percent higher this year than last. I rather concede that under Farmers Home guidelines, delinquency cannot be considered a clear indication of farm bankruptcies, not as long as Farmers Home considers an account delinquent, as I understand it does, if it is $10 overdue and 15 days late in payment. My question is this. Could you provide some data

breakouts showing dollar amounts—for example, how many accounts are delinquent with amounts in excess of $10,000, $20,000, $100,000, or amounts in-between or in excess of these?

Mr. SHUMAN. We will get the best information of that type that we have available, Senator.

[The following answer was received by the committee.]

Our present data system does not stratify delinquent borrowers by amount.

Senator JEPSEN. Finally, in case things get worse, and I hope they do not—I do not think they will, but in case they do—do you have some type of contingency plan for handling what could be a very serious delinquent problem 9 months from now?

Mr. SHUMAN. The direction we are taking in the agency right now is to work with each of our borrowers on a case-by-case basis, trying to find solutions to whatever the problems the borrowers are having. I do not think that the direction of the agency should be altered from that goal. And we do anticipate that this emphasis on servicing and supervising of our existing caseload will continue to be in effect.

Mr. NAYLOR. Senator, I appreciate your concern. I know the Secretary and I share it, that we look at the future at both ends of the range. As we have assessed the programs and the authorities we have asked, it is my personal belief that with careful coordination with the commercial sector, we can meet all 1982 and 1983 needs, if that be the case. Certainly, it would require us to use all the discretionary authority available to us. We are prepared to do that, if that is necessary to continue to strengthen the American agricultural area. We have made that commitment. It is reflected in what is one of the few areas in the budget that continue to be increased—in the operating loan area, for example—continue to make available forward financing in our emergency lending programs. We are prepared to carry out our responsibility.

Senator JEPSEN. Thank you, Madam Chairman.

Senator HAWKINS. Do you have any statistics that would show us the number of borrowers who do not own the land they farm?

Mr. SHUMAN. That do not own the land of our borrowers?

Senator HAWKINS. Yes.

Mr. SHUMAN. Madam Chairman, I will provide for the record the information that we have on borrower characteristics. I do not think, though, that we capture specific percentages of our borrowers who are strictly tenant farmers.

[The following information was received for the record:]

Our borrower characteristics data does not identify the borrowers who are tenants only or who rent land in addition to that owned.

Senator HAWKINS. You do not keep that.

Mr. NAYLOR. I do not believe so, Madam Chairman. Our information system is a little lacking in some of these details.

Mr. SHUMAN. Madam Chairman, I do have available the total number of loans that we had made through March 31, 1982. We have made 52,271 farm loans including farm ownership loans in this fiscal year.

Senator HAWKINS. But in response to my first question, you do not keep that information?

Mr. SHUMAN. No.

Mr. NAYLOR. Madam Chairman, the computer system that is being replaced and being upgraded at this time does not have that kind of management information and data readily available. It becomes a very complex problem and has been for a number of years. Mr. Shuman can provide some of that data on a one-time basis, and in some cases, we can pull it together. But much of the management information which would be helpful to this committee and would be helpful to us within the Department and to Mr. Shuman and his agency simply is not available.

Senator HAWKINS. I know you inherited many problems when you took charge of that Department over there, Mr. Shuman. The lending programs compounded the existing problems. But do you have any goals that you have established for Farmers Home in the first year?

Mr. SHUMAN. Yes, we certainly did have.

Senator HAWKINS. Other than survival. [Laughter.].

Mr. SHUMAN. Well, I guess maybe, if that was one of my goals, I have survived pretty near a year, because it was about a year ago when I came on, so maybe if that was one of my goals, that one has been accomplished.

Yes, I do have some goals. The number one goal, as I have mentioned several times in this testimony here today, is to make the agency more conscious, more aware, of the needs that we have to provide financial management assistance, financial counseling advice to all of our borrowers.

A second goal that I have—and this is maybe a little too nitty-gritty, but as Secretary Naylor indicated, we do have a crying need, a horrendous need for more adequate data processing capabilities, and that is one of our high priorities and one of the very, very important needs in the agency.

A third goal that I have, in our making of new loans, in all of our program areas, is to direct the attention of the agency toward the more truly rural areas of the country. So the three goals, then, that I might list would be, one, continue the direction we have started towards emphasizing supervision and servicing, the need to provide financial management advice and counseling to our borrowers; two, to improve our data processing capabilities; and, three, continue the effort that we have started toward directing the activities of the agency toward truly rural areas of the country.

Senator HAWKINS. You brought up the computer system, which we ran into a lot in preparing for this hearing. I know the agency scrapped one system called the unified management information system. What progress are you making in this direction, and when do you expect to have a workable system on line?

Mr. SHUMAN. Our plans now are in three stages. The first need that we have is to keep the present system that we have now trying to meeting our needs operating through at least another 12 or 13 months. We have made some changes in our present operation that are going to, I think, allow us to survive during this 12 or 13 months. During this 12- or 13-month period, we are converting this system that we have now to a larger, more modern, newer system, with more storage and more processing capability. That will give us about 3 to 4 years of growth, as far as that system and storage capability is concerned. During that 3- or 4-year period we

intend to develop a more modern data processing system to handle our accounting needs.

We hope as a result of the newer system, the management information needs of the agency will be available to us on a more current basis.

Senator HAWKINS. Is this a used system, or is it going to be a new system?

Mr. SHUMAN. You are talking about the third step?

Senator HAWKINS. Yes.

Mr. SHUMAN. It is a development effort, and whether or not it would be an effort that would result in improving what we have in place now or a brandnew system, we have not made that decision yet. It would be a decision based on what would be most cost effective to the Government. The interim steps are using existing equipment, so we have no big new purchase of new hardware. We are taking a look at and are making some changes in programing our software capabilities.

Senator ZORINSKY. Would the Senator yield?

Senator HAWKINS. Surely.

Senator ZORINSKY. You are making the same statement that your predecessor made 2 years ago at this same table, under the Democratic administration, and I hope that the light at the end of the tunnel is more brilliant for your estimation than it was for his.

Senator HAWKINS. That technology changes so rapidly. Technology is advancing so rapidly we can hardly keep up with it, and one generation to the next means the next 6 weeks. Now that I can buy one to put in my utility room, maybe I could help you out.

Senator ZORINSKY. We could buy the Falkland Islands for what this system is costing us.

Senator HAWKINS. Are they for sale? Could we get a loan? [Laughter.]

I am just concerned, as Senator Zorinsky has experienced. I read with interest the 13 hearings you held when you were chairman of this subcommittee, and this is no new problem. But there is new technology, and it is so rapid, from the time I first looked at one this year. They changed the model that I thought I had made up my mind for, and I am hopeful that you do not run into that same problem.

Senator ZORINSKY. They are waiting for an Atari. [Laughter.]

Mr. SHUMAN. Madam Chairman, there may be one very significant difference here between what was stated 2 years ago and the present situation, and that significant difference, I think, is the level of recognition in the Department of Agriculture and the attention that high-level management is paying to the progress that we are making in the agency toward achieving these deadlines and goals. Monthly, Secretary Naylor and others at the Secretary level gather to hear and oversee that operation.

Senator HAWKINS. Have you had any outside help, or are you trying to do this all in-house?

Mr. SHUMAN. There is considerable contracting going on.

Senator HAWKINS. Long term?

Mr. NAYLOR. Madam Chairman, I think your points are well made, and we make some conscious decisions, and I would like to share a couple of observations with you. It is becoming incredibly

difficult within the Federal establishment, and that includes Congress and the congressional system itself, to bring a new data processing system on line. There are an incredible number of hoops that one has to jump through in order to do anything which is one of the problems, I think, the prior system ran afoul of, along with a number of others. With that in mind, we made a conscious decision not to try anything new or exotic, but to use established technology, use established capabilities, to as quickly as we could correct the technical problems with which we were faced. That lessens the number of hoops; it saves us a lot of contracting, outside services, purchasing, bidding, award problems that we get into that seem interminable in the length of time they take, and under the best of conditions which should take 20 or 30 days, and in the private business sector can easily take 6 months to 1 year.

But our business requirements are no different and no less demanding in the private sector, and those kinds of delays are absolutely destructive to our efforts to try and make progress. So we have taken a very conservative approach. We are not trying anything fancy, we are not trying anything exotic. We are just chugging along, but with a very tight schedule and a very conscious effort to get that system cleaned up.

Senator HAWKINS. When this computerized management system is on-line—it is a buzz word up here—would it be possible to assess penalties to farmers with delinquent loans?

Mr. SHUMAN. That could be something that we could consider if the statutes would provide it. At the present time, making any kind of change in our program to do that kind of work would be very, very difficult to accomplish.

Senator HAWKINS. How would you feel about the creation of a pilot project to determine the overall feasibility of a Farmers Home loan program administered by the private sector?

Mr. NAYLOR. Madam Chairman, I think probably we have that in effect in many respects. We are working on that project in the form of the farm credit system, which is a cooperative banking system that originally evolved out of being a Federal agency. There are some aspects, the gray area, which I think you are addressing, where the two systems do not exactly meet up, and there is some overlap, or lack of overlap, there. There are some areas that perhaps we could do more in. There are some areas that perhaps the Farm Credit System could do more in.

I think it is fair to assess what opportunities are available in the Farm Credit System, the services it is rendering. The Farm Credit System is expanding as a result of the Farm Credit Act of 1980, and there are some new services and opportunities available to help farmers that are being provided through that legislation. They are just now coming on line. I do not think they have had a chance to be observed. Certainly, the commercial lending system has been more cooperative than it has been in the past.

I would be hesitant, frankly, candidly, to inject perhaps another layer within that system. We have got three tiers in effect now. But certainly, it is not a subject that should be closed. We should continually review what we are delivering and how we are doing it.

Senator HAWKINS. One final question—and there are a lot of questions here. Senator Helms gave me a stack he would like to

ask you, and I am sure that the Senators probably will want to ask questions for the record. We are getting so interested in the topic that we may not get through today. But I would like to submit these questions that we do not have time to ask for Senator Helms and other Senators that may wish to do so, and ask one final question, and then Senator Zorinsky can have his 10 minutes to finish you guys up.

[The following questions from Senator Hawkins and the Department's answers thereto were subsequently received by the committee:]

*Question.* The administration has recommended that the alcohol production facility loan program be terminated. I understand there have been substantial problems with business failures and loan losses in this program.

Can you please elaborate for the subcommittee on the rationale behind the termination of this program?

Answer. FmHA has obligated about $250,000,000 in alcohol fuel production-type loan guarantees under the Business and Industry loan program. We are currently experiencing problems in four of the smaller projects where original loans of about $1,600,000 were guaranteed. To date, there have been no losses paid in connection with these loans, partially due to the fact that these loans were made in fiscal year 1980 and 1981. Many of these plants are still under construction.

We believe there are sufficient tax and other Government subsidies available to help the private sector finance alcohol fuel facilities projects, so we are recommending termination of the program.

*Question.* There have been suggestions that a "recapture" provision would enable the Farmers Home Administration to recover the difference between its cost of money and the interest paid by low resource farmers on long-term ownership loans when assets are liquidated.

I know you would like to completely eliminate low resource subsidies, but if Congress decides to retain them, how would you feel about including a "recapture" provision in this reauthorization?

Answer. Any recapture provision would need to be structured so that the requirement would not destroy a farmer's retirement plans or interfere with FmHA's graduation requirements.

*Question.* The administration has indicated that it would like to eliminate the interest subsidy currently given to low resource farmers and have all Farmers Home borrowers pay at least the cost of money to the Government. Given the tight credit conditions that are expected in the next year, the expense of interest is of great concern. There have been suggestions that variable interest rates, or sliding-scale interest rates might be considered as alternatives to the current method of determining rates.

As you know, variable interest rates are one method of easing the high cost of money once interest rates begin to come down, and at the same time will keep the Government subsidy in line with the rates paid by farmers who borrow in the private sector. Sliding scale rates would increase with the farmer's ability to pay until the farmer graduated from the FmHA system.

What consideration have you given to these types of interest formulas and how would you view inclusion of provisions such as these in the reauthorizations?

If the low resource loan program is to be completely phased out, how would the administration view the creation of a new farmer program which provided low interest loans only to those individuals just entering farming?

Answer. FmHA is known as the lender of last resort. FmHA borrowers have a high debt load as compared to farmers using other sources of credit. Therefore, FmHA borrowers must use a larger share of their income to pay debts. A rapid increase in a variable interest rate would seriously jeopardize a borrower's repayment ability. Also, during periods of falling interest rates, variable interest rates tend to remain higher than the market rate due to the cost of money the lender has borrowed in the past at the higher rates. The present system of cost of money rate gives some stability to the borrower's costs. Planning is easier with this system. A variable rate system would require a more costly sophisticated accounting and billing system. A sliding scale rate would be very difficult to administer due to the great number of variables involved and the difficulty in obtaining accurate production, income and operating expenses on an individual case basis.

A dual interest rate program is very difficult to administer. Everyone wants the lower interest rate. Not all individuals entering farming need a low interest rate loan. Due to the difficulty of obtaining accurate production and operating records, it is difficult to plan for interest rate increases. Marginal repayment ability can be completely eliminated by an increase. Subsidized interest rates are costly to the Government and the taxpayers.

*Question.* What actions have you taken in the last year to improve administration of the business and industrial program and what assurance can you provide the subcommittee that these actions will result in fewer delinquencies?

Answer. Actions: 1. Major amendments to the B&I regulations which include: (a) Publication in January 1982 of:

(1) A clear definition of equity in a project and what constitutes equity. This change increases tangible equity in the project.

(2) A clarification of when and how debt refinancing can be used.

(3) Clarification of use and requirements of personal and corporate guarantees.

(b) A major revision adding loan servicing sections is being added to the regulations.

2. Numerous other regulation changes are in process which will eliminate loopholes and vague regulation provisions which have caused considerable confusion on the part of borrowers, lenders and FmHA personnel.

3. The Agency has established a system of nationwide assessment reviews to monitor the loan portfolio and administration of the program.

4. All loan applications are now being reviewed in the National Office prior to loan approval.

5. Loan approval authority to the States will be redelegated in accordance with the State's ability to administer the program.

6. Allocation of funds to the States has been changed based upon an updated formula.

7. A desk guide to loan servicing has been developed and distributed to the States.

8. The authority to contract and a contract has been offered for loan servicing expertise from the private sector to help service the entire loan portfolio.

Actions taken such as outlined above and those in process are the result of past experience with administering the program and are all designed to improve the program along with the result of fewer delinquencies.

*Question.* Last year, the House Committee on Appropriations' survey and investigative staff concluded that the minimum 10 percent equity requirement was too low to assure quality loans.

Do you agree with this observation?

Would an increase in the equity requirement lower the risk of default to the Treasury?

Answer. We agree that the minimum 10 percent equity requirement it too low to assure quality loans under certain circumstances. For example, new and unproven business enterprises need at least 25 percent equity to assure success. However, for established businesses with proven successful histories, the 10 percent equity requirement is sufficient.

We think that current legislation is flexible enough to permit the Agency to vary equity requirements to fit individual circumstances and minimize risk of default by the borrower.

*Question.* The House Investigative Committee staff also pointed out that the large dollar losses in liquidated loans were attributable in part to a lack of, or inadequate collateral.

If Congress were to reauthorize this program, what changes could you suggest to correct this problem?

Would a change in this requirement affect the administration's position on eliminating the program altogether?

Answer. In section 324(d) of Subtitle C, pertaining to emergency loans, the act now provides that the Secretary shall rely on "confidence in the repayment ability of the applicant," as well as on hard collateral, in approving a loan. Security requirements could be strengthened by deleting that phrase. The Agency is in the process of deleting that same provision from administrative regulations that pertain to security requirements in farm operating loans. The Agency also is adopting a more prudent and cautious approach to appraisal of real property offered as loan security, in view of a recent decline in the sale value of property that had been appraised at high inflationary values of recent years. Regulations are in the process of being revised to require that property offered as security be appraised on the basis of sales of comparable property within the past 12 months.

These considerations are not essential to the question of whether programs should be continued. They bear more on the quality of program administration and on avoiding borrowers drifting into unmanageable debt.

*Question.* The House Investigative Committee staff also criticized lender servicing of business and industrial loans and recommended that when FmHA is requested to honor a guarantee an audit be performed to determine the loss. If negligence by a private lender was found to be present, the staff recommended FmHA should deny liability.

What has the administration done to implement this recommendation? In addition, if FmHA's loan guarantee were reduced to 80 or 85 percent of the loan, would this result in better lender servicing and if so, would this affect the administration's decision to terminate this program?

Answer. FmHA regulations require that an audit be done to determine loss. If a lender is found to be negligent, FmHA will deny liability, depending on the circumstances.

We have new regulations in the process of being published that define negligent servicing. By defining negligent servicing in the Lender's Agreement, we will be able to more readily determine when a lender has been negligent in servicing, thereby enabling us to be in a better position to not pay for a loss when negligent servicing is evident.

In addition, we have instituted a procedure whereby the National Office reviews all final reports of loss. As part of this procedure, the State Office is required to submit to the National Office an analysis of the loan, including a full explanation of the loss to be paid.

We are in the process of not paying losses or part of the losses on 18 loans on which we have determined the guarantee not to be enforceable.

If FmHA's guarantee rate was reduced to 80 or 85 percent, it is possible that better lender servicing would result, because the lender would be more at risk. We believe the amount of the guarantee should be determined after reviewing specific information on each specific project with emphasis toward reducing the guarantee in all practical cases.

*Question.* It has been suggested that the FmHA's current "credit elsewhere test" could be more stringently applied to keep farmers who can really afford private-sector credit from becoming borrowers from FmHA.

What exactly is the procedure for establishing there is no other credit available for a farmer when he comes to Farmers Home for a loan?

Answer. FmHA Farmer Programs (FP) Loan procedures require the following steps to determine the test for credit elsewhere:

1. All FP loan applicants are required to certify in writing that they are not able to obtain credit elsewhere.

2. The FmHA County Supervisor must investigate and determine whether or not the applicant can get credit elsewhere. Such determinations are made after the County Supervisor contacts other lenders or has current knowledge of other lender programs concerning their loan requirements. The findings and contacts are documented in the running record.

3. The local FmHA County Committee must review each application and reference letters and certify as to whether or not the applicant is able to obtain credit needs elsewhere.

*Question.* For several years the Office of the Inspector General of the USDA has reported that many of the Farmers Home Administration's difficulties servicing loans are the result of a large disparity between the size, number, and complexity of FmHA loan programs and the size and skill of its staff.

In 1980, the OIG, the Undersecretary for Rural Development, and the Administrator of the FmHA, developed over 60 recommendations for improving management of the Farmers Home Administration. These recommendations applied particularly to improving the business and industrial and emergency loan programs.

Again in 1980, the OIG criticized the management of the FmHA and the programs of susceptibility to fraud, waste, and abuse.

After all these reports, recommendations and reviews, can you tell me how you view the problem of staffing and managing the FmHA and what, if any, steps this administration has taken to solve the problem?

Answer. The administration is currently undergoing a reorganization process designed to improve Agency staffing problems within the program areas.

Currently, all loan applications for the B&I program are being reviewed in the National Office prior to loan approval. This is one method designed to improve administration of the program while the reorganization is being implemented at the field level.

There is a comprehensive revision of the program regulations currently in process designed to improve both the loan making and loan servicing processes. These changes are planned for implementation during the current fiscal year. While the above mentioned program "adjustments" will not solve the B&I problems during the immediate future, they are steps in the right direction and will benefit during the long term.

The business and industry (B&I) loan guarantee program, which in a very short time grew to over $1 billion a year, has largely served its purpose. When it was begun in 1974, there was little rural business credit available. Industry had not yet recognized the benefits of locating in rural areas. National migration was toward the larger cities. Today, the situation has reversed. Accordingly, the administration has requested that the program be terminated.

We believe that private investment, not public sector pump-priming, should and will increase development in this area.

The Farmers Home Administration (FmHA) has received criticism for its management of the emergency (EM) disaster loan program from various sources, including hearings held October 17, 1979, by the Senate Subcommittee on Agriculture of the Committee on Appropriations; hearings held October 19, 1979, by the House of Representatives; Subcommittee on Conservation and Credit of the Committee on Agriculture, Conference Report 96-533, dated October 24, 1979; and the General Accounting Office report, CED-78-118, dated May 25, 1978, and CED-79-13 dated August 6, 1979.

In complying with a Congressional mandate that the program be tightened up, FmHA revised its EM regulations effective February 13, 1980. Several items including eligibility and security requirements, were revised in the instruction to correct deficiencies and restore fiscal control to the program. In addition, legislation was signed into law on October 13, 1980, (P.L. 96-438), placing loan limits on the program.

Regulations were further revised in May 1981, to further tighten the program so that it would be directed to those disaster victims truly in need of Federal assistance.

The Administration has recently reviewed the makeup and function of the FmHA District Offices. As a result of this review, some District Offices will be closed and the remaining will be realigned for more effective use. The Personnel from closed District Offices will be assigned to other needed positions in FmHA. FmHA District Directors will spend more of their time supervising FmHA County Offices, giving greater emphasis to Farmer Program loans. FmHA State Directors have been given authority to hire temporary employees to meet the potential workload in the County Offices that expect large numbers of EM applications. The State Directors also have authority to contact with qualified and experienced farm loan specialists for EM loan making and loan servicing when such additional help is warranted.

*Question.* As I understand the present law, although limited resource borrowers receive subsidized loans, these borrowers eventually pay FmHA's regular interest rates as their repayment ability improves.

When this occurs, would these borrowers then be in a position to pay any fees or charges?

If these fees or charges become a burden on the borrower might it be possible to increase the amount of the loan to cover any fees or charges levied by Farmers Home?

Answer. The limited resources loan program has provided beginning farmers and other farmers who lack adequate resources an opportunity to financially compete with established farmers until they can become soundly established in farming. Once a limited resource farmer is able to pay the regular interest rates, it would be self-defeating to place the farmer at an economic disadvantage with other farmers by imposing fees, charges, or additional indebtedness upon him considering the state of the farm economy.

[The following questions from Senator Helms and the Departments answers thereto were subsequently received by the committee:]

*Question.* So far this fiscal year, through March 15,535 farmers had been accommodated through subordination of FmHA liens, as compared to 25,980 given operating and ownership loans. Subordinating represents 37 percent of the action taken to date in this area of lending outside the disaster emergency program.

Would you provide for the record the most current State-by-State allocation list for FmHA Loan and grant programs?

**Answer.** We are providing for the record the fiscal year 1982 State-by-State allocation of loan funds for insured and guaranteed operating and farm ownership loan funds.

## FARM OWNERSHIP ALLOCATION—FISCAL YEAR 1982

[In thousands of dollars]

| State | Total | 1st quarter | 2nd quarter | 3rd quarter | 4th quarter | Sum |
|---|---|---|---|---|---|---|
| Insured: | | | | | | |
| Alabama | 15,400 | 6,050 | 3,850 | 3,850 | 1,650 | 15,400 |
| Alaska | 200 | 79 | 50 | 50 | 21 | 200 |
| Arizona | 3,800 | 1,493 | 950 | 950 | 407 | 3,800 |
| Arkansas | 19,500 | 7,661 | 4,875 | 4,875 | 2,089 | 19,500 |
| California | 12,200 | 4,793 | 3.050 | 3.050 | 1,307 | 12,200 |
| Colorado | 8,300 | 3,261 | 2,075 | 2,075 | 889 | 8,300 |
| Connecticut | 3,200 | 1,257 | 800 | 800 | 343 | 3,200 |
| Delaware | 2,600 | 1.021 | 650 | 650 | 279 | 2,600 |
| Florida | 8,500 | 3,339 | 2,125 | 2,125 | 911 | 8,500 |
| Georgia | 14,800 | 5,814 | 3,700 | 3,700 | 1,586 | 14,800 |
| Hawaii | 1,900 | 746 | 475 | 475 | 204 | 1,900 |
| Idaho | 14,200 | 5,579 | 3,550 | 3,550 | 1,521 | 14,200 |
| Illinois | 29,900 | 11,746 | 7,475 | 7,475 | 3,204 | 29,900 |
| Indiana | 22,800 | 8,957 | 5,700 | 5,700 | 2,443 | 22,800 |
| Iowa | 33,800 | 13,279 | 8,450 | 8,450 | 3,621 | 33,800 |
| Kansas | 25,300 | 9,939 | 6,325 | 6,325 | 2,711 | 25,300 |
| Kentucky | 23,300 | 9,154 | 5,825 | 5,825 | 2,496 | 23,300 |
| Louisiana | 11,900 | 4,675 | 2,975 | 2,975 | 1,275 | 11,900 |
| Maine | 4,900 | 1,925 | 1,225 | 1,225 | 525 | 4,900 |
| Maryland | 6,700 | 2,632 | 1,675 | 1,675 | 718 | 6,700 |
| Massachusetts | 3,400 | 1,336 | 850 | 850 | 364 | 3,400 |
| Michigan | 15,600 | 6,129 | 3,900 | 3,900 | 1,671 | 15,600 |
| Minnesota | 29,100 | 11,432 | 7,275 | 7,275 | 3,118 | 29,100 |
| Mississippi | 17,200 | 6,757 | 4,300 | 4,300 | 1,843 | 17,200 |
| Missouri | 33,600 | 13,200 | 8,400 | 8,400 | 3,600 | 33,600 |
| Montana | 10,100 | 3,968 | 2,525 | 2,525 | 1,082 | 10,100 |
| Nebraska | 25,600 | 10,057 | 6,400 | 6,400 | 2,743 | 25,600 |
| Nevada | 1,200 | 471 | 300 | 300 | 129 | 1,200 |
| New Hampshire | 1,400 | 550 | 350 | 350 | 150 | 1,400 |
| New Jersey | 4,400 | 1,729 | 1,100 | 1,100 | 471 | 4,400 |
| New Mexico | 4,900 | 1,925 | 1,225 | 1,225 | 525 | 4,900 |
| New York | 12,500 | 4,911 | 3,125 | 3,125 | 1,339 | 12,500 |
| North Carolina | 22,200 | 8,721 | 5,550 | 5,550 | 2,379 | 22,200 |
| North Dakota | 22,800 | 8,957 | 5,700 | 5,700 | 2,443 | 22,800 |
| Ohio | 17,300 | 6,796 | 4,325 | 4,325 | 1,854 | 17,300 |
| Oklahoma | 26,100 | 10,254 | 6,525 | 6,525 | 2,796 | 26,100 |
| Oregon | 9,100 | 3,575 | 2,275 | 2,275 | 975 | 9,100 |
| Pennsylvania | 14,100 | 5,539 | 3,525 | 3,525 | 1,511 | 14,100 |
| Puerto Rico | 8,000 | 3,143 | 2,000 | 2,000 | 857 | 8,000 |
| Rhode Island | 2,000 | 786 | 500 | 500 | 214 | 2,000 |
| South Carolina | 8,600 | 3,379 | 2,150 | 2,150 | 921 | 8,600 |
| South Dakota | 21,500 | 8,446 | 5,375 | 5,375 | 2,304 | 21,500 |
| Tennessee | 19,700 | 7,739 | 4,925 | 4,925 | 2,111 | 19,700 |
| Texas | 33,800 | 13,279 | 8,450 | 8,450 | 3,621 | 33,800 |
| Utah | 4,300 | 1,689 | 1,075 | 1,075 | 461 | 4,300 |
| Vermont | 4,500 | 1,768 | 1,125 | 1,125 | 482 | 4,500 |
| Virginia | 10,400 | 4,086 | 2,600 | 2,600 | 1,114 | 10,400 |
| Virgin Islands | 1,600 | 629 | 400 | 400 | 171 | 1,600 |
| Washington | 9,400 | 3,693 | 2,350 | 2,350 | 1,007 | 9,400 |
| West Virginia | 5,400 | 2,121 | 1,350 | 1,350 | 579 | 5,400 |
| Wisconsin | 26,400 | 10,371 | 6,600 | 6,600 | 2,829 | 26,400 |
| Wyoming | 4,000 | 1,571 | 1,000 | 1,000 | 429 | 4,000 |
| W. Pacific | 1,600 | 629 | 400 | 400 | 171 | 1,600 |
| Reserve | 5,000 | 1,964 | 1,250 | 1,250 | 536 | 5,000 |
| Total, United States | 700,000 | 275,000 | 175,000 | 175,000 | 75,000 | 700,000 |

## FARM OWNERSHIP ALLOCATION—FISCAL YEAR 1982—Continued

[In thousands of dollars]

| State | Total | 1st quarter | 2nd quarter | 3rd quarter | 4th quarter | Sum |
|---|---|---|---|---|---|---|
| Guaranteed: | | | | | | |
| Alabama | 1,500 | 600 | 600 | 300 | 0 | 1,500 |
| Alaska | 750 | 300 | 300 | 150 | 0 | 750 |
| Arizona | 750 | 300 | 300 | 150 | 0 | 750 |
| Arkansas | 3,500 | 1,400 | 1,400 | 700 | 0 | 3,500 |
| California | 750 | 300 | 300 | 150 | 0 | 750 |
| Colorado | 1,500 | 600 | 600 | 300 | 0 | 1,500 |
| Connecticut | 1,500 | 600 | 600 | 300 | 0 | 1,500 |
| Delaware | 750 | 300 | 300 | 150 | 0 | 750 |
| Florida | 1,500 | 600 | 600 | 300 | 0 | 1,500 |
| Georgia | 1,500 | 600 | 600 | 300 | 0 | 1,500 |
| Hawaii | 1,500 | 600 | 600 | 300 | 0 | 1,500 |
| Idaho | 750 | 300 | 300 | 150 | 0 | 750 |
| Illinois | 7,500 | 3,000 | 3,000 | 1,500 | 0 | 7,500 |
| Indiana | 1,500 | 600 | 600 | 300 | 0 | 1,500 |
| Iowa | 750 | 300 | 300 | 150 | 0 | 750 |
| Kansas | 750 | 300 | 300 | 150 | 0 | 750 |
| Kentucky | 1,500 | 600 | 600 | 300 | 0 | 1,500 |
| Louisiana | 4,250 | 1,700 | 1,700 | 850 | 0 | 4,250 |
| Maine | 750 | 300 | 300 | 150 | 0 | 750 |
| Maryland | 1,500 | 600 | 600 | 300 | 0 | 1,500 |
| Massachusetts | 1,500 | 600 | 600 | 300 | 0 | 1,500 |
| Michigan | 5,000 | 2,000 | 2,000 | 1,000 | 0 | 5,000 |
| Minnesota | 4,500 | 1,800 | 1,800 | 900 | 0 | 4,500 |
| Mississippi | 2,250 | 900 | 900 | 450 | 0 | 2,250 |
| Missouri | 7,000 | 2,800 | 2,800 | 1,400 | 0 | 7,000 |
| Montana | 750 | 300 | 300 | 150 | 0 | 750 |
| Nebraska | 4,500 | 1,800 | 1,800 | 900 | 0 | 4,500 |
| Nevada | 750 | 300 | 300 | 150 | 0 | 750 |
| New Hampshire | 750 | 300 | 300 | 150 | 0 | 750 |
| New Jersey | 1,500 | 600 | 600 | 300 | 0 | 1,500 |
| New Mexico | 1,500 | 600 | 600 | 300 | 0 | 1,500 |
| New York | 2,250 | 900 | 900 | 450 | 0 | 2,250 |
| North Carolina | 5,000 | 2,000 | 2,000 | 1,000 | 0 | 5,000 |
| North Dakota | 6,500 | 2,600 | 2,600 | 1,300 | 0 | 6,500 |
| Ohio | 1,500 | 600 | 600 | 300 | 0 | 1,500 |
| Oklahoma | 3,000 | 1,200 | 1,200 | 600 | 0 | 3,000 |
| Oregon | 1,500 | 600 | 600 | 300 | 0 | 1,500 |
| Pennsylvania | 1,500 | 600 | 600 | 300 | 0 | 1,500 |
| Puerto Rico | 750 | 300 | 300 | 150 | 0 | 750 |
| Rhode Island | 750 | 300 | 300 | 150 | 0 | 750 |
| South Carolina | 1,500 | 600 | 600 | 300 | 0 | 1,500 |
| South Dakota | 4,500 | 1,800 | 1,800 | 900 | 0 | 4,500 |
| Tennessee | 750 | 300 | 300 | 150 | 0 | 750 |
| Texas | 750 | 300 | 300 | 150 | 0 | 750 |
| Utah | 750 | 300 | 300 | 150 | 0 | 750 |
| Vermont | 1,500 | 600 | 600 | 300 | 0 | 1,500 |
| Virginia | 750 | 300 | 300 | 150 | 0 | 750 |
| Virgin Island | 750 | 300 | 300 | 150 | 0 | 750 |
| Washington | 750 | 300 | 300 | 150 | 0 | 750 |
| West Virginia | 1,500 | 600 | 600 | 300 | 0 | 1,500 |
| Wisconsin | 7,500 | 3,000 | 3,000 | 1,500 | 0 | 7,500 |
| Wyoming | 750 | 300 | 300 | 150 | 0 | 750 |
| W. Pacific | 750 | 300 | 300 | 150 | 0 | 750 |
| Reserve | 15,000 | 6,000 | 6,000 | 3,000 | 0 | 15,000 |
| Total, United States | 125,000 | 50,000 | 50,000 | 25,000 | 0 | 125,000 |

# OPERATING LOAN ALLOCATION FISCAL YEAR 1982

[In thousands of dollars]

| State | Total | 1st quarter | | 2d quarter | 3d quarter | 4th quarter | Total insured |
|---|---|---|---|---|---|---|---|
| | | Guaranteed | Insured | | | | |
| Insured and guaranteed: | | | | | | | |
| Alabama | 26,300 | 960 | 4,961 | 18,180 | 2,027 | 172 | 25,340 |
| Alaska | 500 | 30 | 136 | 218 | 116 | 0 | 470 |
| Arizona | 6,700 | 240 | 1,479 | 3,390 | 1,390 | 201 | 6,460 |
| Arkansas | 36,700 | 1,330 | 6,165 | 23,832 | 4,613 | 760 | 35,370 |
| California | 20,400 | 740 | 4,034 | 10,018 | 4,396 | 1,212 | 19,660 |
| Colorado | 17,500 | 640 | 2,976 | 9,911 | 3,973 | 0 | 16,860 |
| Connecticut | 5,300 | 190 | 1,385 | 1,321 | 1,809 | 595 | 5,110 |
| Delaware | 2,000 | 70 | 397 | 917 | 510 | 106 | 1,930 |
| Florida | 21,300 | 770 | 6,553 | 10,225 | 686 | 3,066 | 20,530 |
| Georgia | 39,200 | 1,430 | 15,321 | 21,912 | 537 | 0 | 37,770 |
| Hawaii | 1,300 | 50 | 318 | 489 | 169 | 274 | 1,250 |
| Idaho | 31,600 | 1,150 | 6,792 | 15,360 | 7,208 | 1,090 | 30,450 |
| Illinois | 47,500 | 1,730 | 9,092 | 23,431 | 11,462 | 1,785 | 45,770 |
| Indiana | 39,300 | 1,430 | 6,231 | 17,704 | 12,061 | 1,874 | 37,870 |
| Iowa | 69,100 | 2,510 | 15,500 | 33,650 | 14,712 | 2,728 | 66,590 |
| Kansas | 38,400 | 1,400 | 7,694 | 16,619 | 10,088 | 2,599 | 37,000 |
| Kentucky | 41,500 | 1,510 | 9,501 | 16,080 | 9,811 | 4,598 | 39,990 |
| Louisiana | 51,700 | 1,880 | 10,442 | 35,005 | 4,373 | 0 | 49,820 |
| Maine | 13,300 | 480 | 1,965 | 3,271 | 7,106 | 478 | 12,820 |
| Maryland | 9,500 | 350 | 1,777 | 3,943 | 2,690 | 740 | 9,150 |
| Massachusetts | 6,000 | 220 | 992 | 1,528 | 1,733 | 1,527 | 5,780 |
| Michigan | 32,900 | 1,200 | 7,023 | 11,455 | 10,495 | 2,727 | 31,700 |
| Minnesota | 56,800 | 2,070 | 11,200 | 24,309 | 16,290 | 2,931 | 54,730 |
| Mississippi | 38,400 | 1,400 | 6,504 | 21,806 | 7,204 | 1,486 | 37,000 |
| Missouri | 56,300 | 2,050 | 10,400 | 30,316 | 12,369 | 1,165 | 54,250 |
| Montana | 16,200 | 590 | 3,425 | 8,788 | 3,397 | 0 | 15,610 |
| Nebraska | 40,600 | 1,480 | 6,183 | 23,226 | 9,911 | 0 | 39,320 |
| Nevada | 1,800 | 70 | 254 | 1,031 | 440 | 5 | 1,730 |
| New Hampshire | 2,400 | 90 | 673 | 621 | 575 | 441 | 2,310 |
| New Jersey | 6,000 | 220 | 1,015 | 3,152 | 1,558 | 55 | 5,780 |
| New Mexico | 9,100 | 330 | 1,661 | 5,584 | 1,400 | 125 | 8,770 |
| New York | 30,900 | 1,120 | 7,443 | 8,867 | 9,087 | 4,383 | 29,780 |
| North Carolina | 58,000 | 2,110 | 25,053 | 26,563 | 2,540 | 1,734 | 55,890 |
| North Dakota | 35,200 | 1,280 | 7,693 | 15,079 | 9,933 | 1,215 | 33,920 |
| Ohio | 22,600 | 820 | 4,399 | 7,337 | 8,122 | 1,922 | 21,780 |
| Oklahoma | 49,400 | 1,800 | 13,338 | 19,606 | 8,363 | 8,293 | 47,600 |
| Oregon | 15,000 | 550 | 4,087 | 7,412 | 2,587 | 364 | 14,450 |
| Pennsylvania | 30,600 | 1,110 | 6,440 | 9,222 | 9,963 | 3,865 | 29,490 |
| Puerto Rico | 9,900 | 360 | 2,197 | 2,999 | 2,622 | 1,722 | 9,540 |
| Rhode Island | 600 | 30 | 69 | 334 | 155 | 12 | 570 |
| South Carolina | 19,800 | 720 | 4,589 | 13,182 | 976 | 333 | 19,080 |
| South Dakota | 42,000 | 1,530 | 9,538 | 18,702 | 10,017 | 2,213 | 40,470 |
| Tennessee | 35,300 | 1,280 | 6,349 | 18,726 | 7,226 | 1,719 | 34,020 |
| Texas | 106,600 | 4,150 | 27,994 | 60,163 | 8,153 | 6,140 | 102,450 |
| Utah | 6,500 | 240 | 1,741 | 2,795 | 1,400 | 324 | 6,260 |
| Vermont | 6,900 | 250 | 1,743 | 1,740 | 2,085 | 1,082 | 6,650 |
| Virginia | 17,000 | 620 | 3,715 | 8,074 | 3,826 | 765 | 16,380 |
| Virgin Islands | 500 | 30 | 180 | 37 | 239 | 14 | 470 |
| Washington | 18,600 | 680 | 3,799 | 10,458 | 3,223 | 440 | 17,920 |
| West Virginia | 9,000 | 330 | 2,362 | 3,075 | 2,170 | 1,063 | 8,670 |
| Wisconsin | 56,900 | 2,070 | 15,514 | 18,969 | 13,690 | 6,657 | 54,830 |
| Wyoming | 7,600 | 280 | 1,983 | 4,404 | 933 | 0 | 7,320 |
| W. Pacific | 300 | 30 | 100 | 100 | 70 | 0 | 270 |
| Reserve | 10,000 | 0 | 2,625 | 4,864 | 2,511 | 0 | 10,000 |
| Total, United States | 1,375,000 | 50,000 | 315,000 | 660,000 | 275,000 | 75,000 | 1,325,000 |

*Question.* Would a deferral on payments and a moratorium on foreclosure benefit marginal farmers by allowing an extension to farm borrowers for one additional year?

How would a loan repayment moratorium be perceived by farm borrowers with loans outstanding from other lenders?

Answer. FmHA presently exercises its authority to defer payments for up to 3 years. Such deferrals provide temporary cash flow relief for some FmHA borrowers. It has little beneficial effect for borrowers who cannot meet their family living and farm operating expenses or who have serious management problems that cannot be resolved through supervision. The cash flow advantages associated with a deferral are short-lived because the deferred interest and principal becomes due and payable and is not forgiven at the end of the deferral period.

A mandatory moratorium on all foreclosures would not benefit borrowers or the FmHA. Under present FmHA regulations and policies, we will continue with all borrowers who have: (1) acted in good faith, (2) made an honest effort to pay, (3) applied recognized successful management practices, (4) accounted for all loan security and (5) have a reasonable chance to repay their 1982 production loan.

Customers of other creditors would perceive that FmHA borrowers who receive a loan repayment moratorium received a temporary financial advantage over them.

[The following question from Senator Zorinsky and the Department's answer thereto were subsequently received by the committee:]

REOPENING OF THE ECONOMIC EMERGENCY PROGRAM

*Question.* Mr. Shuman, would you describe any recent discussions you may have had with your legal counsel regarding the reopening of the economic emergency loan program? And, is it your view that even when it is apparent that an economic emergency exists, reopening of the economic emergency program is still within the Secretary's discretionary authority?

Answer. I am familiar with several discussions that were held between the representatives of the Secretary's Office, members of my staff and representatives of the Office of the General Counsel (OGC) concerning the guidelines that were issued by the Secretary on March 15, 1982, for reopening the economic emergency (EE) loan program.

It is my view that the Secretary intends to exercise his authority to make EE loans available where needed. As you are aware, the Secretary has the discretionary authority—subject to statutory and procedural requirements—to make a particular loan to an applicant.

Senator HAWKINS. How much have you done to subordinate the Government liens so that the farmers not eligible for more Farmers Home credit can get production loans from other lenders?

Mr. SHUMAN. We have had tremendous success in that area, Senator. We have about twice the number of subordinations so far this year that we had at the same point last year, and really appreciate the cooperation that the private sector has given us in that regard.

Senator HAWKINS. So, the statistics that we have demonstrate a willingness to cooperate with you.

Mr. SHUMAN. They do. They demonstrate a tremendous response, I think, by the private sector to the Secretary's appeal to them in early January.

Senator HAWKINS. Senator Zorinsky.

Senator ZORINSKY. Thank you, Madam Chairman.

Secretary Naylor, it is my understanding that the Office of Management and Budget has said that the Farmers Home Administration delinquencies will be reduced by 70,000 in 1983. As a matter of fact, OMB attributes $4 billion in budget savings to this and other similar efforts. Because it was included in the President's budget, I assume this reduction is a quota, not a goal—not that there is that much difference between a quota and a goal. But did OMB set this

quota after consulting with the Farmers Home Administration, and how will the Farmers Home Administration reach the quota set by OMB?

Mr. NAYLOR. Senator, I would not call that a quota. It probably might more appropriately be a strategy goal. But it was not limited simply to farmlands. It also dealt with housing and all loans by the agency, and as you are aware, the vast majority of our loans are housing loans in just sheer numbers—over 1 million. I would not think that goal in the housing area alone would be very difficult to achieve, just set aside agriculture off to one side.

In terms of bringing accounts current—and I think that is something we continually have or appear to have, and perhaps we need to do a better job—a communications problem. Bringing an account current has the same effect as closing out an account, as far as bringing it to date. Our objective has been and continues to be to work with our borrowers under supervision to bring their accounts current and help them keep them current as a matter of good financial management and practice. I think it is a doable thing, particularly in the housing area. At the same time, we recognize that there will be situations where it simply cannot be done, and particularly, that is true in the farming area this year. Where that is the case, we have and will continue to use all the discretionary authority available to us, to reschedule, reamortize, or any of the other authorities, to help these producers carry forward.

Senator ZORINSKY. Well, did OMB consult with you to arrive at this 70,000 figure? Why isn't it 80,000? If 70,000 is good, 80,000 is better.

Mr. NAYLOR. Senator I think it was developed based on some data that they had seen from our own work within the agency, and the answer is no. I do not think we were directly consulted. I think it was based on some estimates of data that had been worked on within the agency, particularly in the housing program area.

Senator ZORINSKY. I see. So they took the raw data and computed their figures without coming back to you and saying, is this realistic?

Mr. NAYLOR. As you know, that budget preparation, particularly the notes, which is where that came from, are developed rapidly. The numbers as a goal, particularly if you put them in the perspective of the housing side of our operation, where we have over a million borrowers, I am not sure that that is not a very realistic goal from that perspective. Certainly, it would be more difficult in the farming area, and we have used to great length our discretionary authority to help those producers where they cannot bring it current.

Senator ZORINSKY. Thank you.

Charlie, as I understand the new regulations for the water and waste disposal loan program, there would be three interest rates—5 percent for poverty level communities, 8⅝ percent for communities with 85 percent or less of the statewide, nonmetropolitan median family income, and 12⅜ percent for the remaining communities. In Nebraska there are only two counties that would qualify for the 5-percent loans, and there are a larger number of counties in many States that supposedly qualify for the 8⅝-percent loans. However, as you know, the Farmers Home Administration has a policy that

limits the percent of income that can be used to pay water and waste disposal bills. I believe this policy is known as the 1-percent rule. The problem is, in order to comply with the 1 percent rule, a community that qualifies for an 5⅝-percent loan would have to keep the project cost per user below $6,000. And in the sparsely populated areas of western Nebraska, the per user cost is frequently $8,000 or more. Assuming that you comply with the congressional directive to direct grant funds to the lowest income communities, how do you propose to assist the hundreds of communities that are affected by this unique and specific mathematical problem?

Mr. SHUMAN. I think you are addressing, Senator, our criteria for determining the amount of grant funds an applicant is eligible for.

Senator ZORINSKY. Yes.

Mr. SHUMAN. The interest rate determination is separate from that. The interest rate that would be used in amortizing the bonds, that determination is made separate from the way in which we determine the amount of grant funds that might be available. Incidentally, those same regulations that carried the new interest rates also carried with it the new determination for grant funds. So the two, tied together, I think, eliminate the problem that you are addressing.

Incidentally, also, the interest rate is not specifically set at certain percentages. The second interest rate is half way between the market interest rate and the 5-percent interest rate. The market interest rate and the second or intermediate rate would vary from quarter to quarter.

Senator ZORINSKY. Do you feel that that does resolve the fact that many communities are concerned that they might fall between the cracks because of the 1-percent rule?

Mr. SHUMAN. No, Senator, I do not think we are going to have any communities fall between the cracks. There will be a way to determine the interest rate for any one of the communities. We have said that our grant funds are going to be going to the lower income communities. There may or may not be grant funds available, but the interest rate would still be determined by the income of the average resident.

Senator ZORINSKY. We were concerned that the per user cost is obviously higher in a sparsely populated community as opposed to a more densely populated community, which would mean that their triggering mechanism would be at $8,000 per user, the project cost, as opposed to $6,000 which would have qualified them.

Mr. SHUMAN. I will check with technical staff specifically and deal with it further for the record, but I do not think there is a problem.

[The following response was subsequently received by the committee:]

Under the proposed new FmHA regulations, the grant determination would not be based on construction cost per user, but rather on percentage of debt serviced in relation to median family income.

The following describes the proposed regulations:

An application will be considered for grant assistance only when the debt service portion of the average user cost for either water or waste service, for only those

users in the applicant service area, exceeds the following percentages of median family income:

1. .5 percent when the median family income of the service area is below the OMB poverty line for a nonfarm family of four.
2. 1.0 percent when the median family income of the service area is not more than 85 percent of the statewide nonmetropolitan median family income.
3. No grant funds will be used for any project where the median family income of the service area is more than 85 percent of the statewide nonmetropolitan family income.

Senator ZORINSKY. Thank you, Charlie.

In the essence of time, Madam Chairman, I do have some more questions, but I would like to ask unanimous consent that I submit them for answers in writing, and also, on behalf of Senator Huddleston and Senator Boren, to submit their statements as having been submitted at this hearing, in addition to questions from Senator Huddleston and Senator Borne, with requests to have them answered in writing.

Senator HAWKINS. Without objection.

[The following questions from Senator Huddleston and the Department's answers thereto were subsequently received by the committee:]

FAMILY FARMS

*Question.* A recent report on the status of family farms stated that the number of middle-sized family farms continued to decline and that, if the trend continues, American agriculture could be left with essentially two major classes of farms: large farms, producing most of the output, and small farms, producing little and maintained primarily as rural residences.

The Farmers Home Administration limited resource farmer programs were developed to help young beginning farmers. The administration is proposing the elimination of those programs. If the administration proposal is adopted, won't it be more difficult for many young and beginning farmers to get started?

Answer. The family farm is still the most efficient farm and is providing the majority of the agriculture products in the United States. However, they are becoming larger. There are very few large corporate farms with the stock owned by investors rather than family members and friends. We have had proposals from several sources that, due to the large surplus of dairy and poultry products, FmHA should declare a moratorium on starting new or beginning farmers in these enterprises. There are large surpluses in many of the farm commodities. We are working very hard to save the farmers already established.

However, we believe that good capable young farmers can get started farming without the limited resource programs. We can start them out as tenant farmers with operating loans with deferred payments for the purchase of livestock and/or equipment and operating expenses. They will have less debt and a chance to gain experience and equity. We also have a pilot program to furnish additional services to borrowers under the "New Full-time Family Farmers and Ranchers Development Committee." We think this will be a great aid to beginning farmers. Many young farmers start out as part-time farmers.

NATURAL DISASTER PROGRAM CAP

*Question.* I understand that the administration is proposing a cap of $1.54 billion for the natural disaster loan program in fiscal year 1983. I believe that last year at this time the administration estimated that $1.6 billion would be needed for this program for 1982. I understand that the Farmers Home Administration has already exceeded that estimate for 1982. What is the new estimate for 1982?

In view of the record, and since it is obvious that natural disasters can't be predicted, wouldn't such a cap on this program in fiscal year 1983 be irresponsible?

Answer. The latest approved apportionment anticipates a $1.9 billion disaster loan level during fiscal year 1982. The $1.54 billion loan level should be sufficient unless there are major unforeseen needs to be dealt with by supplemental authority.

REAMORTIZATION AND RESCHEDULING

*Question.* On February 11, 12 other members of this committee and I sent a letter to Secretary Block asking him to change Farmers Home Administration policy to allow reamortizing and rescheduling of farm loan repayments at the original rate of interest agreed to at the time the loan was obligated. I haven't yet received an answer to that letter. Also, on March 31, the committee agreed to include in H.R. 2160 (a bill the committee is reporting to the Senate) a sense of Congress resolution that makes a similar recommendation.

Could you comment on the recommendations that have been made by this committee?

Answer. 7 CFR Part 1951, subpart A prescribes the procedure for reamortizing and rescheduling loans. This regulation is currently being revised (which will permit rescheduling and reamortizing of farm loans at the original interest rate or the current interest rate, whichever is less). We will publish this regulation as a final rule as soon as practicable.

DISASTER DESIGNATIONS

*Question.* As I understand the natural disaster designation procedure, the administration has removed local designation authority from the Farmers Home Administration State Director and centralized it here in Washington. There is an exception: A State director may designate a county as eligible for assistance if fewer than twenty-five farmers are involved.

Doesn't this policy create a gap in cases where there may be forty or fifty farmers in a county who have suffered severe damage to crops, but the county as a whole doesn't qualify for a national designation because of your stringent standard denying designation to a county unless there is a 30 percent loss countywide? What course of action is available to such farmers?

Answer. You are correct in your understanding that the disaster designation procedure has been changed. Disaster designation can be made by the President, the Secretary, and in cases of 25 or less farmers substantially affected, the FmHA State Director can make emergency loans available.

"Substantially affected" has been determined to be a 30 percent loss to all crops growing in an area, including hay and pasture. The 30 percent criteria has been used as a guideline and is used along with other information submitted by county and state Emergency Boards, in determining whether or not an area needs emergency loan assistance.

SHORTAGE OF OPERATING LOAN FUNDS

*Question.* Recently, Secretary Block said that not a single farmer would be turned away from the Farmers Home Administration because of a shortage of operating loan funds. However, I have heard reports that several State Farmers Home Administration offices have requested additional operating loan funds. How many States have requested, or advised you, that additional operating loan funds are, or may be, needed? Is it true that some States will be required to return part of their allocation of operating loan funds in order to ease the shortage in other States?

Answer. Following a normal pattern, the demand for operating loans is greater in some states and not as great in some other states. To date we have increased the insured operating loan allotments in 4 states and decreased the allotment in 8 states. The supply of operating loan funds in the 8 states exceeded their demand and they voluntarily released part of their allocations to states experiencing a shortage of funds. We will continue to ask states that are not using their funds to release part of their allocations to ease the shortage in other states. As usual, the extent of designations for emergency loans is a factor in the need for operating loans.

FARM CREDIT SYSTEM

*Question.* Recently, representatives of certain farm credit system districts have indicated that they expect to turn down up to 10 percent of their past borrowers this year, and perhaps another 10 percent next year. Many of these farmers have never borrowed from the Farmers Home Administration. Will the Farmers Home Administration be able to assist these farmers if they turn to that agency for financing?

Answer. Each application will be evaluated on its own merit. If these Farm Credit borrowers are denied further credit from the Farm Credit System because of poor management, production capability, or other factors that will limit their repayment ability, FmHA may not be able to assist them. It is anticipated that FmHA will

graduate some borrowers to other credit sources and we should be able to assist additional borrowers.

SUBORDINATION

*Question.* The Farmers Home Administration has been accepting a subordinated position on farm loans for some time. The additional emphasis this administration has given that policy is commendable. However, in my State of Kentucky, only 31 borrowers have benefited from this policy this year. Isn't the significance of this policy being exaggerated? Would subordination be more widely used if the commercial lender was not responsible for collection costs if the loan is foreclosed?

Answer. Nationally, a substantial amount of credit from other sources in lieu of additional FmHA credit is assisting many borrowers. Reasonable liquidation costs can be released from sales proceeds.

We do not feel the significance of our subordination policy is being exaggerated. It is a very vital and useful financial tool which can benefit our borrowers, other agricultural lenders and FmHA.

In some cases, administrative costs, such as collection of defaulted loans, are factors that may have restricted the acceptance of FmHA subordinations; however, the Agency does not intend to absorb all such costs in an effort to achieve a greater acceptance to this policy. We feel the borrower will receive better supervision and the account will be more thoroughly serviced if the lender has to share some risk.

PAST ECONOMIC EMERGENCY LOAN BORROWERS

*Question.* The Farmers Home Administration estimates that about 10,000 past economic emergency loan borrowers are above the regular operating loan program limit. Therefore, they are presently unable to get credit from the Farmers Home Administration. Almost all of these borrowers are unable to get credit elsewhere. What alternative do these farmers have besides the economic emergency loan program?

Answer. We recognize that FmHA will not be able to make operating (OL) loans to some indebted EE loan borrowers because they operate larger than family-size farms. A portion of these presently indebted EE borrowers are eligible for emergency (EM) loan assistance and their financial needs can be met with an EM loan. Those borrowers that do not qualify for any type of FmHA loan but do have a sound basis for additional credit will be assisted by FmHA subordinating its security interest to enable indebted EE borrowers to obtain their operating credit from other lenders. Additionally, FmHA will continue in justifiable cases to exercise its rescheduling, reamortization, and deferral authorities to assist indebted FmHA EE borrowers to continue their farming operations.

DECLINE OF BLACK FARMING

*Question.* A February 1982 report, issued by the U.S. Commission on Civil Rights, was critical of the Farmers Home Administration in regard to the assistance being provided to black farmers. The report states that Farmers Home Administration may have actually hindered the efforts of small black farm operators to remain viable.

Please provide the committee with FmHA's response to the report including any recommendations contained in the report that have been adopted.

Answer. FmHA's response to the report was made to the Secretary's Office on April 12, 1982. Our response, submitted for the record, includes a response to the recommendations in the report.

APRIL 12, 1982.

To: John Schrote, Acting Assistant Secretary for Administration.
Subject: U.S. Civil Rights Commission Report: "The Decline of Black Farming in America."

Attached is the Farmers Home Administration's response to the subject report and its recommendations. As I understand it, FmHA's material will be incorporated into an overall departmental policy to the Chairman of the Civil Rights Commission. Our reply includes a general commentary of the reasons, as FmHA sees it, for the decline in Black farming in the United States and comments on those recommendations applicable to FmHA.

CHARLES W. SHUMAN, *Administrator.*

## Response to Civil Rights Commission Report, "The Decline of Black Farming in America"

The Farmers Home Administration has a good deal of sympathy for the concerns raised in the report, "The Decline of Black Farming in America." The decline of the black ownership of farmland, we agree, has hindered the efforts of one sement of our population to remain a viable force in agriculture. It is important to recognize, however, that many of the issues raised by the report have less to do with Farmers Home Administration programs and policies than with the broad trends in agricultural economics.

Let us review some of the trends in agriculture, mentioned in the report, that impact adversely on black and other small farming operations independent of FmHA programs:

(a) Historically, black farmers have experienced a competitive disadvantage due to the relatively small size of their land holdings. The land, often more poorly located and less fertile than white owned property, cannot support needed loans because of low appraisals and even lower productive capacity. The result is that limited productive capacity reduces income levels and smaller loans are approved.

(b) New technology for large scale farming and agricultural research have to a great extent worked to the disadvantage of small famers. Equipment, for example, resulting from research is often more expensive per acre to operate than the average black farmer can afford. These costs have an adverse impact on small farm operations, and the amount of credit black farmers can afford to carry.

(c) Because of labor intensive operations requiring minimum outlays of capital and machinery, small farmers often are not able to benefit from a tax structure that rewards capital investment. Large operators, on the other hand, are encouraged to expand and turn away from labor intensive to capital intensive operations through tax incentives.

(d) Government farm prices and support programs, which have been tied to volume of production, provide the least benefits to small operators. Participation in commodity programs, for example, has helped large farm operators to obtain credit that allowed them to invest in land, and agriculture technology. By being able to expand the operations, large farmers have been able to compete and remain in agriculture.

(e) A perplexing problem associated with black ownership of farmland is that of heir property. Historically, land is passed down through generations among blacks without the benefits of a will, and conveyed among a number of family members oblivious to State Inheritance laws. A study in the report included a sample survey that found 27 pecent of all black owned land was heir property and owned by an average of eight people. With ownership spread among so many individuals, the land becomes susceptible to partition and tax sales. This partition of land ownership has often resulted in the loss of farms by black owners to outside bidders. In addition, lending institutions, including FmHA, encounter great difficulty in making loans on this type of heir property which is needed for security.

A most significant issue raised by the report questions the Agency's failure to use the Limited Resources Loan as a tool to specifically address the needs of black farmers. Since it became a part of our lending authority in 1978, this loan program has been administered to meet the needs of all "family farmers and ranchers who not only cannot get credit elsewhere but cannot afford to pay the normal interest on FmHA loans." It has not been viewed as a black farmer program, but as one to meet the needs of all low-income farmers under dire circumstances.

To aid the Agency in determining whether its position was on firm ground, we asked the Office of General Counsel to research the intent of Congress as it relates to the Limited Resource Loan and black farmers. In a reply dated March 29, 1982, OGC replied: "The statutory language does not mention giving minority farmers any kind of preferential treatment so far as receiving a Limited Resource Loan is concerned."

Since FmHA officials met with the Commission last January, steps have been taken to retrieve data on the racial make-up of Limited Resource Loan borrowers. Though information is not yet available on farm ownership loans, we can report that black farmers received 377 of the 3,765 insured farm operating Limiting Resource Loans advanced through September 30, 1981, and since its inception, the Agency has met or exceeded its goals in advancing these loans.

The report also raised the issue that the Agency lacks an outreach program to blacks and other minorities. We hope to correct that situation in the ensuing weeks ahead. A new statement on outreach is being developed, and we expect it to be the

basis for an outreach program that will reach into the communities of rural America and the grassroots organizations of blacks and other minorities.

RECOMMENDATION

The Farmers Home Administrator should revise FmHA regulations (governing the Limited Resource Loan Program) to ensure that farm loans are provided to those for whom Congress intended. For example, FmHA regulations should:

Provide, for purposes of eligibility, a more specific definition of a "Limited Resource Borrower."

Require documented outreach to minority and small farmers, informing them of special loan programs, particularly the Limited Resource Program.

ACTION TAKEN/PROPOSAL

The Agency has found deficiencies in the Limited Resource Loan instruction and is taking steps to correct them. The revised instruction will clarify eligibility requirements and present a stricter "credit elsewhere" test to insure that only qualified applicants are approved for the Limited Resource Loan. In addition a new FmHA Civil Rights Compliance Instruction, 1940-D, is in draft form. The draft includes a requirement that State Offices report community outreach activities.

RECOMMENDATION

The Agency should insure that county committees are representative of the population of the county which they serve.

ACTION TAKEN/PROPOSAL

The Agency's instruction on the composition of county committees is being revised to provide more guidance and direction to State Directors in making appointments to the committee. The revised instruction will be more precise in its direction so that the State Director's appointments will better reflect the diversity of farm operators in the county, for example, male/female and minority/nonminority farmers. In addition, the Equal Opportunity office will monitor and provide the Administrator with a makeup of county committees. Already, the Equal Employment Opportunity (EEO) staff receives a quarterly computer printout that reports minority/female composition of county committees.

RECOMMENDATION

The Farmers Home Administrator should:

Require that goals for minority participation in FmHA programs, including the Limited Resource Program, be established (prior to the program year) and met at the county level;

Delegate additional adequately trained staff to monitor minority goals and participations, the quality of service and outreach to minorities, and conduct compliance reviews;

Develop specific interpretations of ECOA requirements and establish guidelines for enforcement in FmHA loan programs.

ACTION TAKEN/PROPOSED

FmHA attempts to establish loan goals prior to the beginning of the fiscal year. However, Congress frequently does not appropriate funds until after the fiscal year has begun. It is almost impossible, if not impractical, to set goals when fund allocatioins are unknown. In fiscal 1982, minority loan goals were established and approved by December 1981, which is a vast improvement over the previous fiscal year. State Directors have been, and continue to be accountable for meeting State loan goals. It is impractical to hold them responsible for each *county* meeting its goals since there are a variety of uncontrollable factors, e.g, natural or economic disaster that effect whether an individual county meets its goals.

FmHA is unable to devote more personnel resources to the Civil Rights program at the National Office level. A possible method of strengthening the overall Civil Rights effort, however, it through the use of minority coordinators at the State level. Taking on the responsibilities of coordinator as additional duties, the coordinator, among things, could monitor outreach activities and identify methods to strengthen program delivery to minority farmers. USDA's Soil Conservation Service uses a corp of minority coordinators in its Civil Rights activities.

FmHA's revised Civil Rights training program includes the Equal Credit Opportunity Act, its requirements, and its applicability to FmHA programs. Enforcement criteria will await departmental guidance.

BUSINESS AND INDUSTRIAL LOAN PROGRAM

*Question.* Off-farm income has become more important in recent years as a source of income for farmers. The business and industrial guaranteed loan program has been used to create or save jobs in rural areas by drawing funds from urban financial centers.

(1) How many jobs has the B&I program created or saved?

(2) Have farm families benefited from this program?

(3) For how many loans and for how many total dollars have guarantees been issued?

(4) In how many instances and for what amount has the Farmers Home Administration had to make payments to banks to cover loan losses?

Answer. The Business and Industry program has as its mission the creation and saving of jobs in rural areas.

1. As of December 31, 1981, 136,057 jobs have been created and 137,077 saved for a total of 273,134 jobs.

2. We have no statistics which measure the number of farm families who have benefited from the program. However, since 70 percent of all loans have been made in areas of less than 10,000 population, it can be assumed that a large number of farm families are included in the above percentage due to the rural makeup of the population.

3. As of April 6, 1982, guarantees have been issued for 3,585 loans for a total dollar amount of $3,207,643,644.

4. Through fiscal year 1981 FmHA paid losses totaling $61,315,000.

ALCOHOL FUELS

*Question.* The Farmers Home Administration has been directed by Congress to issue loan guarantees totaling $250 million for alcohol fuel facilities. What is the status of this program? Specifically how many loans have been guaranteed?

Answer. The entire $250 million authorized and mandated by Congress to be used to guarantee for alcohol production facilities loan guarantees is available for fiscal year 1982. As of April 19, 1982, no loans have been guaranteed or conditional commitments issued. However, we have one application in the amount of $8,400,000 under review in the National Office. In addition, there are several other projects in various stages of consideration at the State level.

FIVE-PERCENT WATER AND WASTE DISPOSAL LOANS

*Question.* When the Congress agreed to the administration's request of a year ago that we raise the interest rate for the water and waste disposal loan program, we were assured that about half of the loan funds would be made to lower income communities at the 5 percent rate.

How many 5 percent loans have been made in fiscal year 1982 and what proportion of the total amount of loan funds committed in fiscal year 1982 does this represent?

Answer. From October 1, 1981, to March 31, 1982, the Farmers Home Administration made forty-eight 5 percent loans which represents 8 percent of the total loan funds obligated.

GRANT DETERMINATIONS

*Question.* Could you explain to the committee the process that the Farmers Home Administration uses to determine how much water and waste disposal program grant money will be provided for a specific project?

At what level is this decision made?

How would the regulations you proposed on March 30 affect this procedure?

Answer. Farmers Home Administration (FmHA) regulations presently provide that ordinarily, an applicant will be considered for grant assistance only when the debt service portion of the average user cost for either water or waste service, for only those users in the applicant service area, exceeds the following percentages of median incomes:

(i) .75 percent when the median income is under $6,000.

(ii) 1.00 percent when the median income is $6,000 to $10,000.

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(iii) 1.25 percent when the median income is over $10,000.

FmHA District Directors are responsible for determining applicant eligibility for grants and the amount of such grants.

The proposed FmHA grant regulations published in the March 30, 1982, issue of the Federal Register would change the basis for determining grants. Under the proposal, an applicant would be considered for grant assistance when the debt service portion of the average annual user cost exceeds the following percentage of median family incomes (MFI) on the service area:

(1) .50 percent when the MFI of the service area is below the poverty line.

(2) 1.00 percent when the MFI of the service area is not more than 85 percent of the nonmetropolitan median family income (NMFI) of the State.

(3) No FmHA grant funds will be used in any project when the MFI of the service area is more than 85 percent of the NMFI of the State.

GRANTS TO LOW-INCOME AREAS

*Question.* If all the 5 percent water and waste disposal loans made so far this year have gone to communities with poverty level incomes, how many of the projects involved with these loans also received Farmers Home Administration grant funds?

Answer. From October 1, 1981, through March 31, 1982, the Farmers Home Administration (FmHA) made forty-eight loans at a 5 percent interest rate. Of these loans, twenty-one were accompanied by an FmHA grant.

WATER AND WASTE DISPOSAL PROJECT SELECTION

*Question.* In the conference committee report on last year's Budget Reconciliation Act, the administration was directed to develop a project selection system to use deciding which water and waste disposal projects are to be funded. Do I understand correctly that now, about ten months later, a system hasn't been developed?

Assuming that there are many projects competing for limited water and waste disposal funds, how does the Farmers Home Administration decide which projects receive the little amount of money that is available?

Answer. A more formalized selection system is being developed for use by the states to prioritize projects for processing within the state. Presently projects are selected for water and waste disposal loans based on the priorities contained in Farmers Home Administration regulations. These critiera include public bodies, improvements necessary to comply with the Safe Drinking Water Act, low incomes, populations not in excess of 5,500, unanticipated diminution or deterioration of water supply, inadequate waste disposal facilities and mergers.

USURY LIMITS

*Question.* I understand that several States have usury limits that are lower than the 12⅝ percent interest rate charged by Farmers Home Administration for water and waste disposal loans.

Are you familiar with this program, and how do you propose to address it?

Answer. We understand that no state, without Congressional consent, can regulate any Federal governmental agency, such as the Farmers Home Administration (FmHA), carrying out constitutionally authorized programs of Congress. Therefore, state usury laws will not affect the interest rate set by the Secretary pursuant to section 307(a)(3)(A) of the Consolidated Farm and Rural Development Act, as amended. However, applicants for FmHA's Water and Waste Disposal Loans must comply with state laws that limit their borrowing power. Such state laws would prevent an applicant from borrowing from any source at a rate of interest in excess of a specified amount.

[The following questions from Senator Boren and the Department's answers thereto were subsequently received by the committee:]

FINANCE OFFICE

*Question.* I have several questions that relate to the operation of the Farmers Home Administration's finance office. As you know, the finance office problems affect farmers by delaying checks and failing to credit accounts.

(1) What steps have you taken to alleviate the situation and what is your timetable for resolving the problem?

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(2) Have the Department and the Office of Management and Budget approved the purchase of equipment needed to improve operations?

(3) Has the finance office been authorized any additional personnel to deal with the backlog?

(4) When the new system is in place, will the farmers home administration be able to provide detailed information on borrower characteristics?

Answer. (1) An immediate action we have taken is to "fast track" farm production-type loans through the Finance Office. Such loans are identified when they enter the office and given higher processing priorities at each step to assure getting the checks in the hands of the farmer as rapidly as possible.

The Farmers Home Administration (FmHA) has developed and is in the process of implementing a plan to improve the performance of the Agency's accounting system.

The growing workload of the accounting system made it necessary to develop both a short-range plan and a long-range plan. The short-range plan addresses those problems that have to be corrected immediately, such as providing adequate data processing capacity for a rapidly growing portfolio. The long-range plan provides for a new accounting system which will be approved by the General Accounting Office (GAO). This new system will also bring the level of office and data processing mechanization in line with general industry trends. Such a plan was developed and has been presented to staff members of several Committees in recent months.

Recently, a new medium scale computer and modern cash processing equipment were installed to allow speedier processing and greater support for the field offices as interim steps.

The first major step in the FmHA plan is a conversion of the current accounts processing from medium scale computer equipment in St. Louis to IBM-compatible large-scale hardware at the USDA Kansas City Computer Center. In addition, the conversion plan includes some much needed enhancements which will make the system viable for 3–5 years. The second major step, which would be completed by 1986, is the design and implementation of a GAO-approved accounting system which will improve service to the borrower and to management. These efforts are under separate project management under the overall leadership of the Assistant Deputy Administrator for Automated Systems Development. These efforts are being managed in-house and use a combination of in-house personnel and contract assistance to optimize the effectiveness of the efforts. Key milestones associated with these efforts are presented below:

SCHEDULE OF ACTIONS

Conversion of two small systems as a pilot operation, June 1982.

Development of data base for the converted accounting system, September 1982.

Converted accounting system installed, mid-1983.

First phase of long-range system design completed (user needs validated, delivery system identified and costed out, accounting functional work completed and presented to GAO), May 1983.

Second phase—longer-range system design completed, June 1984.

Third phase—long-range system development completed, September 1985.

Redesigned and GAO-approved system installed, March 1986.

(2) Yes, thus far we have received excellent support. In fiscal year 1983 we have requested $550,000 for additional automated data processing equipment; $350,000 of these funds will be used for remote job entry equipment for batch data transmission between the St. Louis Finance Office and the Kansas City Computer Center. The remaining $200,000 is for computer terminals and controllers in the St. Louis Finance Office to provide access to borrower account information.

(3) Yes, the Finance Office has been provided additional personnel to handle the backlogs in depositing borrower loan payments and updating borrower accounts. This issue is being monitored and adjustments are being made dependent on need and budget availability.

(4) Yes, however, the nonfinancial portions of this information are currently under development in the Management Information System Development Division. The new accounting system will also bring the level of office and data processing mechanization in line with general industry trends in providing this type of financial information.

FORECLOSURE POLICY

*Question.* I am concerned about the number of FmHA farm borrowers who are in jeopardy of having their loans foreclosed. A few months ago, this committee was as-

sured by the administration that the number of foreclosures would not substantially exceed the level of past years. We were told that about 300 foreclosures per year was typical. I understand that the number of forced liquidations and so-called voluntary liquidations is now near 2,000 for this fiscal year. I know this is a small percentage of the total borrowers, but, does that represent a substantial increase from past years? How have you communicated your foreclosure policy to the county offices? Are county supervisors' performance ratings dependent on any sort of delinquency goal or quota?

Answer. The Agency maintained no reporting system in past years to tabulate borrower liquidations for reasons other than foreclosure. A reporting system was established by the present administration at the beginning of fiscal year 1982. It shows that for the period of October 1, 1981, through March 31, 1982, among FmHA borrowers, 198 liquidations by foreclosure were completed; 981 liquidated their operations prior to completion of foreclosure; 1,012 other borrowers in financial difficulty liquidated their operations voluntarily. Farmers with active loan accounts on March 31 totaled 262,189. Foreclosures completed represent 7/100ths of one percent, other liquidations 7/10ths of one percent of total borrowers.

The foreclosure policy now being exercised by the departmental and Agency administration has been fully communicated to County Offices, primarily through State Directors, in operational directives to the field.

Evaluation of County Supervisors' performance in servicing delinquent loans takes into account economic conditions in a supervisor's servicing area, and the degree to which delinquency is caused by conditions beyond the borrowers' control.

COOPERATION WITH BORROWERS

*Question.* As you know, the FmHA County Supervisor has a good deal of discretionary authority and this authority can be used to either assist, or in some cases hinder, the operations of a borrower. I know that the tremendous workload is a strain on the county offices. However, despite the pressures, County Supervisors are public servants and should act in the best interest of the agency and the borrower regardless of the personal feelings of the supervisor. Have you taken any specific steps to assure greater cooperation between borrowers and County Supervisors?

Answer. Each FmHA employee is required to give faithful service to the public. We have sent numerous policy statements to all County Supervisors which provide guidance for county office personnel in the handling of borrower's subsequent loan requests and the servicing of existing accounts. On November 8, 1978, FmHA initiated an administrative appeal procedure which provided a uniform procedure for borrowers or applicants to appeal adverse actions. All FmHA employees have been instructed to conduct themselves in a courteous and professional manner when dealing with the public.

PROCEEDS FROM SALES

*Question.* Farmers Home Administration presently requires its borrowers to turn over proceeds from sales of assets and mineral lease royalties, which are to be applied against the final loan repayments. What is the rationale for applying these proceeds to the back end of the loan as opposed to the current obligations of a farmer? Are these cases where a borrower might be required to turn over proceeds of a sale or royalties to the Farmers Home Administration and be turned down by the Farmers Home Administration for an additional loan because the agency lacks funds?

Why is the borrower required to obtain another loan when these proceeds or royalties could be used to finance operations?

Answer. Farmers Home Administration identifies income from security property as either normal income derived from sales of production and increase or income from sale of basic security. Normal income can be used to make payments on debts falling due, pay operating and family living expenses, replace essential items or carryover for next year's operation. Repayment ability of a borrower is based on normal income.

*Basic security* sales are a depletion of the security property. Chattel proceeds may be used to replace items sold with like or more suitable property or applied on debts for which the property is pledged as security. Real estate proceeds may be used to develop or enlarge the farm or applied on debts for which the property is pledged as security.

Mineral lease income can be treated as normal income but royalty payments are derived from actual sale by removal from the property and considered sale of basic security. This may be a minor detriment to a farm serving as security when oil and

gas are sold. A small surface acreage is usually disturbed for location, roads and lines. A major detriment would exist for surface mining of coal, gravel, or other such minerals. Proceeds are applied as extra payments since they are depletion of security property and beyond the normal income used to establish the borrower's repayment ability. When major reductions of a note occur, a reamortization of the debt can be completed if needed to reduce the annual installment.

Since FmHA clearly separates and identifies normal income and basic security in accordance with source of income, it would be possible for a borrower to be required to reduce the real estate secured note from sale of royalties or land and need operating credit for annual expenses.

The borrower is required to obtain a loan for operating purposes or real estate purposes as authorized by the appropriate loan authority. For example: operating loans are not authorized to purchase real estate; farm ownership loans are not authorized for annual operating expenses.

HIGH INTEREST RATES

*Question.* We are all aware that one of the main reasons our farmers are facing difficulties is because of the high interest rates. Farmers are simply unable to pay such high interest rates and stay in business. In light of this, can you explain to me why you have failed to alter existing policy to allow rescheduling at the original rate?

Answer. The rescheduling of FmHA farm loans at the original rate is being given serious consideration. We are considering alternatives which will permit rescheduling at the original interest rate or the current interest rate, whichever is less.

Senator HAWKINS. I would like to ask one final question that we need answered. In processing loans, Farmers Home performs a number of services, as I understand—making credit checks, appraisals of security, management assistance and counseling, construction and security inspections, tax—monitoring services, loan servicing and processing, and graduation reviews; is that correct?

Mr. SHUMAN. That and other things. You have pretty well named all of the things that are involved in both loan-making and loan-servicing. There could be some argument on the breakdown and some other things may be involved there.

Senator HAWKINS. Senator Zorinsky is a specialist in this, because he has been involved in it for so long, and I am in the learning process. Does Farmers Home authority allow it to levy fees or charges for any of those services?

Mr. NAYLOR. I am sure it is very limited authority, Senator. Let me check that for the record.

Mr. SHUMAN. We do have some limited authority in that way, and I would be glad to look into it and explain to you for the record the specific programs.

[The following response was received for the record:]

Under general administrative provisions of the statutes there is authority for establishing fees and charges for FmHA services.

Senator HAWKINS. I understand there is a charge for a Farmers Home credit report.

Mr. SHUMAN. That is correct.

Senator HAWKINS. And I would like a report from you that we could distribute to all members of the committee if there are any charges that Farmers Home makes and what is the rationale for charging or not charging.

Mr. NAYLOR. We will be glad to do that for the record.

[The following information was received by the committee:]

The FmHA does not impose fees or make charges for services provided to applicants and borrowers. The imposition of fees and charges would be a further burden

on farmers and other rural residents who are coming to FmHA as a last resort credit source and generally or moderate to lower income families.

Borrowers do pay certain services not performed by FmHA such as credit reports, lien searches, title checks and insurance and other attorneys fees.

Senator HAWKINS. Thank you so much. We have tons of questions for you, and in answering them, it is a pity you cannot use your computer system. [Laughter.]

Mr. SHUMAN. Madam Chairman, one of these days you will be recommending that we do just the opposite, that we answer them with our computer system.

Senator HAWKINS. I hope so. Thank you.

Mr. NAYLOR. Madam Chairman, thank you so much. It has been a pleasure to appear before your subcommittee. And thank you, Senator Zorinsky, for your assistance and comments and questions. We look forward to answering those for the record and will continue working with this committee very closely.

Senator ZORINSKY. Thank you, and thank you for the job you are doing under such trying circumstances.

Senator HAWKINS. Thank you for coming.

Our next witness will be Carl T. Frederickson, the Senior Deputy Governor of the Farm Credit Administration.

Mr. Frederickson, if you could condense your statement, we would appreciate it.

## STATEMENT OF CARL T. FREDERICKSON, SENIOR DEPUTY GOVERNOR, FARM CREDIT ADMINISTRATION

Mr. FREDERICKSON. Madam Chairman, Senator Zorinsky, I am C. T. Frederickson, Senior Deputy Governor of the Farm Credit Administration. I do have a statement which has been provided to the committee, and I would like, if you have no objection, to have that filed for the hearing record, and I will make a few very brief comments.[1]

The Farm Credit Administration, as I think you know, is an independent agency in the executive branch. Our job is to supervise, regulate and examine the institutions of the Farm Credit System. The System is composed of Federal land banks and Federal land bank associations, the Federal intermediate credit banks and PCA's and the banks for cooperatives. The land banks make long-term first mortgage loans to farmers and ranchers and presently hold about 42 percent of the total long-term credit outstanding to agriculture. The production credit associations, working with the FICB's, make short and intermediate term loans to farmers and ranchers, and they hold about 25 percent of the total short and intermediate term credit outstanding. The banks for cooperatives provide credit service to farmer cooperatives and provide a total of about 65 percent of the total credit outstanding to farmer cooperatives.

Let me make a few comments about the agricultural economy and credit conditions in agriculture, a subject which is of great interest to us all, particularly in these times. We regard the situation as being rather serious in agriculture at the present time. As has already been said here, we are now in the third year, and in some

[1] See p. 98 for the prepared statement of Mr. Frederickson.

areas of the country in the fourth year of declining agricultural income. Net cash income in agriculture last year, 1981, was $19 billion; about another $4 billion in an inventory build-up, for a total net farm income of $23 billion. And we project this year a range of net farm income somewhere between $13 and $18 billion. If it is at the lower end of that range, we would be looking at one of the lowest levels of real agricultural income since the depression years. To give a little better perspective on that, in 1973, the net farm income reached an all-time peak of $33.5 billion. By comparison, a net farm income level in 1982 of $13 billion would, in real terms, be about 20 percent of that.

The agricultural financial condition in the aggregate still is very strong, and it will be strong at the end of this year. Debt as a percentage of total assets for agriculture will still be only slightly over 17 percent. Our concern is the relationship of this debt of $200 billion to net agricultural income. In 1973, net farm income was $33.5 billion and agricultural debt was $100 billion. In that year the ratio of net agricultural debt to income was 3 to 1. That ratio could be as high as 13 to 1 this year.

The Farm Credit System has this past year served more people than ever before in its history. The land bank total loan numbers went up slightly more than 8 percent. The production credit associations' numbers went up less than that, in the range of 2 to 2.5 percent. The total number of PCA and landbank borrowers served is slightly over 1 million at the present time.

The System is experiencing some decline in credit quality as one would anticipate during periods of stress. So far, this decline in credit quality is still well within the manageable range, and we do not expect that situation to change this coming year. We use a four-step rating system to evaluate credit quality. The top rating is "Acceptable", and last year the percentage of the total PCA "Acceptable" loan volume declined from 85.5 of loans outstanding down to about 84 percent, not terribly significant in that regard, and not a matter which causes a great deal of concern at this point.

We anticipate that this year, the decline in that percentage will probably be on the order of 5 to 6 percent, which would make it the sharpest decline in that percentage since 1974 to 1975, and one of the most significant declines in that measure in the System's history. That will still leave the System in a manageable position, but it does indicate that a significant number of borrowers are experiencing a significant amount of stress. Thus far, the System has been able to maintain that quality without the necessity of a great many foreclosures. The System has been able to continue with the vast majority of its borrowers without having to say no, though the incidence of that is increasing and probably will continue to do so, but we think only marginally so.

With that, Madam Chairman, I think I will stop and attempt to respond to questions that you and the Senator may have.

Senator HAWKINS. In your statement before the Senate Budget Committee in March, you stated that agriculture's debt-to-asset ratio looks very good at first glance, and then you pointed out that some 500,000 to 600,000 farmers are leveraged at almost double the national average. Given the low farm income levels and the fact

that interest expenses have risen to 13 percent of total production costs, can you estimate how many farmers now in the Farm Credit System might no longer be eligible for FCS loans at this time next year—a guesstimate.

Mr. FREDRICKSON. That is an extremely difficult question to respond to, because one has to make some assumptions as to what is going to happen between now and next year. If interest rates do decline, if export volume picks up, which would have some considerable impact on commodity prices, if the national economy improves and our net farm income is at the upper end of that $13 to $18 billion range, the number will be negligible; very, very few. If it is at the lower end of that range, we could be talking about some numbers, but I think they would still be small enough that they would not create a great deal of concern yet next year: 1 percent, perhaps, at the very most. That is probably a high estimate.

Senator HAWKINS. On March 23, Governor Wilkinson wrote the chairman of the House Subcommittee on Conservation Credit and Rural Development, describing the nationwide credit monitoring procedure that the Farm Credit Administration has instituted. How is the development of that system proceeding?

Mr. FREDRICKSON. We have one preliminary report, and we anticipate another, which will be due the end of this month. Our system calls for quarterly reporting, and the April 30 report will be the first full fledged report under this credit monitoring system. We think it is going to give us and, in turn, this subcommittee and other committees of the Congress, as needed, information as to what is going on during these particular periods of time in the Farm Credit System.

Senator HAWKINS. In that same letter, the Governor indicated that the Farm Credit System indicated a 3.6 percent delinquency rate on all outstanding loans. Since that time, has there been an indication that the delinquency rate has worsened?

Mr. FREDRICKSON. No, as a matter of fact, the delinquency rate has gone down. Those percentages—and that was for the land bank system—were as of January 31. And January 31 is always the peak date for delinquencies, because we have so many annual payment loans which come due in January, or at the first of the year, and will be delinquent then, if they are ever going to be. Most of those payments have been caught up, or in many cases, the loans have been reamortized, and that percentage now will be back down to a much more normal figure of perhaps 1.5 percent.

Senator HAWKINS. So your figures would be 1.5 percent where the Farmers Home Administration has over half, or 50 percent of its outstanding farm loans delinquent?

Mr. FREDRICKSON. That is true. I am not sure those are very comparable situations, but that is true.

Senator HAWKINS. So that they report in January?

Mr. FREDRICKSON. Yes.

Senator HAWKINS. How does the Farm Credit Administration view the proposed moratorium on repayment of Farmers Home loans?

Mr. FREDRICKSON. As a general proposition, we would not view a moratorium as being a constructive kind of measure. The difficulty with a moratorium on foreclosures, as desirable as the objective ob-

viously is, is the fact that in, at least some circumstances, it would preclude the lender—in this case, the Farmers Home Administration—from taking action which may well be the only remaining action in a situation where there simply is no further hope of success. And it would be our judgment that the Farmers Home Administration has the administrative flexibility to stay with those borrowers who do have an opportunity and some reasonable hope of succeeding, and at least thus far, our observation is that the administration has been doing that.

Senator HAWKINS. So I take it from your statement that the Farm Credit System would never consider imposing a moratorium on its loans?

Mr. FREDRICKSON. We would not.

Senator HAWKINS. You stated in your testimony before the Senate Budget Committee that the Farm Credit System has adopted an attitude of forbearance toward borrowers currently suffering financial hardships and indicated such in your statement today. What specific policy directives or actions has the FCS taken to prevent loan liquidation, either voluntarily or involuntarily?

Mr. FREDRICKSON. Madam Chairman, we have not issued any specific policy directives to the banks. We have consulted with the boards of directors, with managements of the banks. These people understand the situation fully, as well as we do, and perhaps better than we do. We are watching the situation closely to see that they are conducting their lending operations in accordance with this general policy of forbearance. We believe that there is every indication that they are. Just one quick number, to give an indication of that. In February this year, the PCA's total loan extensions were composed of 45 percent renewals of loans already outstanding. On the one hand, this is not the happiest kind of statistic, because it indicates that many farmers have had a considerable amount of difficulty in repaying the loans that they already owe, but I think it does, on the other hand, indicate that the System has been quite responsive in accordance with this policy of forbearance.

Senator HAWKINS. Before the Senate Budget Committee, you also suggested that while farmers are reducing their borrowing for operating loans from the production credit association, borrowing for real estate purchase continues to increase. What explanation do you offer for the reluctance of farmers to incur short-term debt, contrasted with their willingness to continue purchasing land?

Mr. FREDRICKSON. Well, I think the reluctance of farmers to incur short-term debt for operating purposes is fairly easy to understand. The prospects for income are down. Purchases of fertilizer and machinery and inputs of all types are down. Farmers are simply tightening the belt in a very, very significant way. In regard to the purchases of land—we, very frankly, have difficulty ourselves in explaining the basis on which, as many farmers, as continue to do so, are buying land. The pace has slackened very noticeably in the last few weeks. The rate of land transfers has been slowing down. But frankly we have until recently been very surprised at the rate at which farmers have continued to borrow for the purchase of land.

Senator HAWKINS. In recent years, there has been discussion concerning the establishment of a rural development bank as part of the Farm Credit System. How do you feel about that?

Mr. FREDRICKSON. As you indicate, Madam Chairman, proposals of this sort have been surfacing over a long period of time. The System would certainly have no objection at all to—and could perhaps see some merit in the creation of such a rural development bank. However, the System does not think that it would be appropriate for any such rural development bank to be a part of the Farm Credit System.

Senator HAWKINS. The administration proposed eliminating the interest subsidy to low-resource farmers. Taking action of this nature would be consistent with the goal of reducing the cost of this program to the taxpayer, I know, but variable interest rates might be one method to reduce the burden on the taxpayer created by low-interest, long-term loans and still provide flexibility for the borrower. I know that the Farm Credit System utilizes variable interest rates. Would you give me—and maybe Senator Zorinsky already knows that—your views on the positive or negative aspects on variable interest rates?

Mr. FREDRICKSON. Well, the variable interest rate approach has been used by the Farm Credit System for quite a number of years. The Federal land banks now have about 97 to 98 percent of their total loan volume on a variable interest rate plan. All—or essentially all of the PCA and BC loans are on a variable rate plan. Very frankly, the Farm Credit System would likely today be in the same position as many savings and loan associations are in, were it not for the variable interest rate plan. It does have the disadvantage of shifting all of the interest rate volatility risk to the borrower, and there is no way that one can put it any differently than that. On the other hand, it does allow the lending institution to go to market and buy the money that the borrower needs and provide it to him at some price. The price may not be the one he wants to pay, and certainly, today, we are not able to do that, but we are able to stay in business, and we are able to provide credit to farmers during good periods and bad.

Senator HAWKINS. Finally, I am very concerned about the elimination of the limited resource farm loan program that might prevent beginning farmers from entering farming. What has the Farm Credit System's experience been with young farmers, what terms are offered, and what has been the overall result of your operation with these young borrowers?

Mr. FREDRICKSON. The Farm Credit System does not offer any special plans or provisions for young farmers. The System has done a great deal of financing of young farmers, both directly, by itself, and in cooperation with the Farmers Home Administration under various of their loan subordination and participation programs; but the System does not offer any concessional terms to young farmers.

Senator HAWKINS. I have one last question, and then Senator Zorinsky can wrap this up. Farmers Home Administration came under criticism for management inefficiencies and inadequate staffing for the size and complexity of the programs it must administer for as long as I can read the hearings that have been held on this subcommittee. Have you compared the size and the level of an indi-

vidual loan officer's caseload employed by Farmers Home and the Farm Credit Administration? Do you have that, or could you provide it for us?

Mr. FREDRICKSON. Madam Chairman, I do not think we could make that comparison, because we do not know what the ratios would be in the Farmers Home Administration. We could give you a range of what it is in the Farm Credit System. I suspect, when you see those numbers, you are going to be somewhat surprised at the range, because it depends a great deal on the type of agriculture and the type of borrower that is being served in a given area. In one set of circumstances, a given loan officer may very easily be able to handle 100 to 125 loans. In another set of circumstances, if he has 25, he will have more than he can say grace over.

Senator HAWKINS. If you would provide that to us.

Mr. FREDRICKSON. We would be happy to do so.

Senator HAWKINS. We have had a great amount of difficulty getting the statistics or the information that we wanted from Farmers Home, and they have been excused for that, but hopefully, they are improving.

[The following response was received by the committee:]

The table below summarizes the number of System employees. Most, but not all, employees listed as "professionals" are loan officers. As of March 31, 1982 the Farm Credit System had $72,091,225,000 outstanding.

| District | Professional employees | Total permanent |
|---|---|---|
| Springfield | 337 | 626 |
| Baltimore | 437 | 830 |
| Columbia | 897 | 1,949 |
| Louisville | 1,367 | 2,421 |
| New Orleans | 497 | 911 |
| St. Louis | 822 | 1,499 |
| St. Paul | 1,280 | 2,371 |
| Omaha | 1,120 | 1,941 |
| Wichita | 803 | 1,236 |
| Texas | 474 | 856 |
| Sacramento [1] | 155 | 283 |
| Spokane | 573 | 948 |
| Central Bank | 45 | 61 |
| Farmbank | 38 | 56 |
| Fiscal Agency | 16 | 25 |
| Total | 8,861 | 16,012 |

[1] Bank data only. No information is available on the number of association personnel in the Sacramento district.

Senator Zorinsky?

Senator ZORINSKY. Recently, Mr. Fredrickson, the Farmers Home Administration has been giving greater emphasis to accepting a subordinated position on loans. I think this emphasis is commendable, but has there been a significant increase in loan activity by the Farm Credit System as a result of this policy, or are you aware?

Mr. FREDRICKSON. There has been some increase. It has been relatively recent. We have definitely noticed it, and as Secretary Naylor indicated to you earlier, we have been trying in every way to cooperate with Farmers Home Administration. At this point, we do not have any numbers to indicate exactly how much of that in-

crease there has been in terms of numbers alone, but there clearly has been an increase, and we anticipate that that will continue.

Senator ZORINSKY. Mr. Fredrickson, in your opening statement, you made a comment that the statistics that you were providing in the statement indicate that there is a tremendous amount of stress in the agricultural industry today, and you said it is quite evident that this stress exists. From those same figures, would you also go so far as to say there is a tremendous lack of cash flow in the farming sector, also?

Mr. FREDRICKSON. There clearly is, Senator. There clearly is a lack of cash flow. There is a lack of income, and there is a lack of cash flow.

Senator ZORINSKY. Would you like to join with the members that were here at the table previously and the prognosis of what is going to happen in the last two quarters of this year with respect to interest rates and the economy, or do you not wish to get involved in that?

Mr. FREDRICKSON. I would be delighted if we could all wake up on December 31, 1982 and find that the optimism has been entirely justified. In candor, we are not quite as optimistic as that.

Senator ZORINSKY. I appreciate your honesty, your integrity, and I certainly respect that comment. I would like to thank you personally for your appearance here at the hearing, and certainly, I think the Farm Credit System is to be complimented for being a nonburden on the taxpayers of this country. I think many people neglect to realize that factor, that you are a self-sustaining organization, and do a mighty good job at it. Please give my regards to Governor Wilkinson.

Mr. FREDRICKSON. Thank you, Senator. I will be delighted to do that, and thank you for those kind words.

Senator HAWKINS. I join Senator Zorinsky in thanking you for coming, and helping us in this task before us and want to continue to keep in touch with you. You really are a model program in today's real world, even more so than possibly in past years, and I was reading previous hearings conducted by this subcommittee.

This concludes the hearing we have for today. We have others scheduled on this subject as the month goes by and as the year goes by, and we really appreciate your participation.

Mr. FREDRICKSON. Thank you, Madam Chairman.

[Whereupon, at 3:50 p.m., the subcommittee recessed, to reconvene Wednesday, April 21, 1982, at 10 a.m., in room 322, Russell Senate Office Building.]

# REAUTHORIZATION OF FARMERS HOME ADMINISTRATION LOAN LEVELS FOR FISCAL YEARS 1983, 1984, AND 1985

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WEDNESDAY, APRIL 21, 1982

U.S. SENATE,
SUBCOMMITTEE ON AGRICULTURAL CREDIT AND
RURAL ELECTRIFICATION OF THE
COMMITTEE ON AGRICULTURE, NUTRITION, AND FORESTRY,
*Washington, D.C.*

The subcommittee met, pursuant to notice, at 10:10 a.m., in room 324, Russell Senate Office Building, Hon. Paula Hawkins (chairman of the subcommittee) presiding.

Present: Senators Hawkins and Jepsen.

Also present: Senator Pryor.

## STATEMENT OF HON. PAULA HAWKINS, A U.S. SENATOR FROM FLORIDA

Senator HAWKINS. The subcommittee will come to order, please.

Senator Zorinsky is heading this way. The demands on our time are many, as you may know. And at this point in time I am going to ask Senator Jepsen to give his statement since he is due in 10 minutes, in another part of the Senate.

Senator Jepsen.

## STATEMENT OF HON. ROGER W. JEPSEN, A U.S. SENATOR FROM IOWA

Senator JEPSEN. Thank you, Madam Chairman. I regret having to leave this hearing early because of prior commitments. I again commend you for the tremendous service and great work you are doing in holding these hearings.

I ask leave that I might introduce at this time an Iowan who will be testifying later on during the hearing. He is John Hall, of Adel, Iowa, chairman of the rural water task force of the Water Quality Association, and former president of the Iowa Water Quality Association. Mr. Hall is also president of a franchised water improvement equipment dealership in Adel, with branches in Missouri Valley and Sioux City, Iowa.

He is a graduate of the University of Iowa and has been active in the water treatment business for 17 years. Mr. Hall is a native Iowan. He was born and raised in Dallas County.

And, with that, Madam Chairman, I wish you well. I will try to get back: I do have to personally testify at 10:20 on the sixth floor of the Dirksen Building. That is where I have to go now.

Senator HAWKINS. Thank you for coming. I am sure we will be seeing you. We appreciate your interest in this subject. It is most important to America today.

Today the Subcommittee on Agricultural Credit and Rural Electrification will continue its hearings on authorizing the major rural programs administered by the Farmers Home Administration for the fiscal years 1983, 1984, and 1985.

Last week the subcommittee heard testimony from the Under Secretary for Small Community Development, the Administrator of Farmers Home Administration, and a Farm Credit representative.

Today we will hear from groups representing farming, banking and rural communities vitally interested in the decisions Congress will make in Farmers Home programs.

Last week we concentrated on rural credit conditions facing American farmers. And we found that falling rural farm income is a major problem. Despite record crop yields, low commodity prices drove farmers' net income down from $27.4 billion in 1979 to $19 billion in 1981. After adjusting for inflation, this amounted to a 45-percent drop in real income.

In their testimony, both the administration and the Farm Credit Administration indicated that 1982 will be another rough year for the farmers. We discovered, however, that despite low income, overall credit conditions are favorable. Land values, rising rapidly in the last decade, have turned the assets of farmers up by $640 billion more than their debts. That means by 1981, farm assets equaled $1 trillion while farm debts totaled $200 billion.

Clearly though, high interest rates make farming more expensive; however, the farm community as a whole should not have difficulty acquiring credit. Unlike other potential borrowers, farmers have a lot of collateral to offer lenders. But borrowers from the Farmers Home Administration are not typical farmers. They, as a rule, did not own farmland before its price rose and they have insufficient collateral to satisfy the requirements of private lenders. Low commodity prices mean their ability to repay is eroding and, indeed, over half the loans made under programs subject to the subcommittee's jurisdiction are delinquent.

These late payments raise the cost of Government for all taxpayers by reducing Treasury cash balances. The Federal Government must borrow more money than otherwise to finance its operations, increasing total interest charges. Therefore, ways need to be considered to protect taxpayers and farmers in need.

Last week I announced the subcommittee is reviewing such reforms. These include, but are not limited to, charging variable interest rates, depending on ability to pay, and recapturing a portion of the interest from borrowers who sell their land at a profit.

In addition to these reforms, the subcommittee is exploring requiring borrowers to purchase Federal crop insurance. Finally, we may encourage borrowers to use the commodity markets. These proposals could help insure the borrowers had adequate cash flow to repay their loans even if national disasters or economic difficulties strike.

Last week, the subcommittee also reviewed the difficulties Farmers Home is experiencing in installing a comprehensive computer-

ized information management system. I intend to work closely with the administration to get one installed and working.

In today's hearing, the subcommittee will discuss possible changes in the business and industrial loan program. These include raising the equity requirements for business and industrial loans, guaranteeing less than 90 percent of such loans to encourage more careful lending by commercial banks and improve targeting of funds to poverty and jobless areas.

I would also like to look at ways to insure that Government helps the smallest and most rural communities in America, to see that they have adequate water and sewer facilities.

With these thoughts in mind, I would like to call our first panel: Mary Kay Thatcher, assistant director, National Affairs Division, American Farm Bureau; James Miller, assistant director of legislation for the National Grange; Paul Sacia, legislative assistant, National Farmers Union; and James Eatherly, chairman, Agricultural Bankers Division, American Banking Association.

Mr. Sacia is not present as yet. We will start at this time with Ms. Thatcher. Do you have a statement?

## STATEMENT OF MARY KAY THATCHER, ASSISTANT DIRECTOR, NATIONAL AFFAIRS DIVISION, AMERICAN FARM BUREAU FEDERATION

Ms. THATCHER. Madam Chairman, Farm Bureau appreciates the opportunity to present testimony on amendments to the Consolidated Farm and Rural Development Act.

The American Farm Bureau Federation is the Nation's largest general farm organization with a membership of over 3 million families in 48 States and Puerto Rico. Farm Bureau members produce virtually every type of commodity grown on a commercial basis in the country. Farm Bureau policy is developed by the producer members at the county, State, and national levels of the organization.

Farm Bureau is concerned that S. 2314, which sets lending limits for Farmers Home Administration loan programs, does not place enough emphasis on farm ownership and operating loans. With farmers facing a third consecutive year of depressed incomes, we believe that most of the money proposed to fund the water and sewer facility loans, the business and industry loans, and the insured community facility loans should be shifted to farm ownership and operating loans.

Farm Bureau is also concerned about the administration of the business and industry loan program. The B. & I. loan program provides guaranteed loans only and, therefore, serves primarily to reduce the risks for other lending institutions. We support elimination of this program entirely, and would urge the funds and resources presently used for this program be shifted to the operating and ownership loan programs.

Until the B. & I. program is eliminated, we recommend the following options to tighten up the program:

First, reduce the guaranteed level on the loans. Farmers Home now guarantees business and industry loans at 90 percent. This

high level of guarantee encourages bankers to do more loan making than loan servicing.

Second, set a maximum funding limit per project. Presently there is no limit on the amount of business and industry funding which may be given to one project. A maximum limit per project would insure that more projects would receive aid.

Third, increase the equity requirement. The present requirement that a borrower put up only 10-percent equity is outdated in these economic times.

Madam Chairman, I have attached a copy of the Farm Bureau policy regarding the Farmers Home disaster loan program for your reference. Thank you again for the opportunity to testify.

[The following information was received by the committee:]

FmHA Disaster Loans

We believe that Farmers Home Administration (FmHA) disaster loans should be made only to farmers who have suffered an unusual natural disaster and are unable to obtain financing elsewhere.

We believe that FmHA disaster loans should be governed by the following principles:

(1) Interest rates should not be subsidized by the Federal Government.

(2) Interest rates should be variable to reflect the market conditions over the term of the loan.

(3) Letters of loan denial from commercial lenders should be required.

(4) All of the applicant's assets should be considered before a loan is granted.

(5) Any interest subsidy should be recaptured if the farm is voluntarily sold during the term of the loan.

(6) Loans should be reviewed every 2 years and the loan terminated if commercial credit is available.

(7) Borrowers should not be allowed to use the proceeds from a disaster loan for expansion.

(8) All lending institutions which provide agricultural funding should make every effort to reamortize or extend agricultural loans on an individual basis in order to assist farmers affected by natural disasters to stay in business and operate through the 1982 season.

(9) The final decision on the loan should be left to the local governing board.

Senator Hawkins. Mr. Miller.

## STATEMENT OF JAMES MILLER, ASSISTANT DIRECTOR OF LEGISLATION, NATIONAL GRANGE

Mr. Miller. Thank you, Madam Chairman.

My name is Jim Miller. I am assistant legislative director of the National Grange. I have a full statement that I would like to submit for the record.[1] And I will just summarize one or two of the principal points that I would like to make.

Our organization has been watching the Farmers Home Administration for many, many, many years. And there are a number of points that we would like to bring out today and, hopefully, this administration and future administrations will keep track of where the Farmers Home Administration has been, is going, and where it ought to be—keep its eye on the original mission of the Farmers Home Administration.

Our organization also favors elimination of the B. & I. loan program. It is our experience that B. & I. loans, in addition to many of

[1] See p. 109 for the statement of Edward Andersen, president, National Grange as submitted by Mr. Miller.

the housing loan programs, are taking too much time away from those Farmers Home Administration officials out in the field who can adequately supervise and study the farm production issues that are facing American agriculture today.

One of the things that we have been urging, and I think that we are getting a good deal of support from the administration now, is that some Farmers Home Administration loan officers out in the field need increased training in supervision of farm loans. To this point the other loan programs have taken too much time and required special knowledge. And it is our position that farm operating and farm ownership loans, in addition to the supervision of these loans, requires a good deal of background and a good deal of training.

Generally we have been supporting the direction that the current administration has been proceeding with Farmers Home Administration. We are encouraged that the administration is pursuing a course that will graduate certain Farmers Home Administration lenders to conventional sources in a timely and in an orderly fashion.

It has been, and always has been a problem, that certain Farmers Home Administration lenders or borrowers will stay in the Farmers Home Administration's programs beyond that point where it is necessary for them to have established their farming operation. We find it encouraging that these Farmers Home borrowers, once they get established, once they gain a little equity in their property, are encouraged to graduate on to other sources.

We are encouraging that Farmers Home Administration do increase their emphasis in the operation, farm ownership, and farm operating loan programs. These are by far and away the most important loan programs in the Farmers Home Administration, and those that are clearly doing the farmers the most good.

We are asking that the limited resource application program clause be reinserted because we feel that this does perform a vital function for many of those borrowers. And by setting aside a certain percentage—25 percent we felt was a reasonable amount—to target those loans to low-income borrowers we think is the proper role for the Farmers Home Administration to serve.

I would be happy to respond to any questions you might have and we certainly appreciate this opportunity to talk to you.

Thank you.

Senator HAWKINS. Mr. Eatherly.

## STATEMENT OF JAMES R. EATHERLY, CHAIRMAN, AGRICULTURAL BANKERS DIVISION, AMERICAN BANKERS ASSOCIATION

Mr. EATHERLY. Madam Chairman and members of the committee, I am James R. Eatherly, chairman and president of the First National Bank of Tonkawa, Okla. I am testifying today in my capacity as the chairman of the Agricultural Bankers Division of the American Bankers Association.[1] Our association consists of more than 13,000 full-service banks, over 90 percent of the Nation's banking community. Two-thirds of the Nation's full-service banks

[1] See p. 113 for the prepared statement of Mr. Eatherly.

are in communities of less than 25,000 people. According to the latest estimates, over 5,000 of these community banks listed agriculture as the single most important source of income for their communities.

Banks are interested and involved in the agriculture sector of the economy. At the end of 1981, commercial banks provided an estimated $30.4 billion in operating loans to farmers and an estimated $8.97 billion in mortgage loans secured by farmland. These figures are large in both absolute and relative terms and indicate the substantial involvement of banks in farm lending. Much of this farm debt is provided by smaller banks in rural areas.

Thank you, Madam Chairman, for this opportunity to present the association's views on S. 2314, a bill to amend the Consolidated Farm and Rural Development Act. S. 2314 would continue FmHA's farm real estate and production loans at the $2.2 billion level, and would raise the production loan authorization from $1.375 to $1.51 billion a year. It proposes a ceiling of $1.54 billion on the disaster emergency authorization, and provides for loan authorizations of $300 million for water and waste disposal project loans, $130 million for loans to finance other community facilities in rural communities that have no other sources of assistance.

The bill does not request authorization to continue the business and industrial loan guarantee program; and would terminate authority for nonemergency farm loans at subsidized interest rates. The American Bankers Association supports S. 2314. We believe, however, that the issues involved in this legislation need to be considered in a somewhat broader context. Specifically, we believe that the operation of the Farmers Home Administration should be examined in relation to the whole structure of this country's financial institutions and the credit needs of the agricultural sector of the economy.

Of the major public agencies that lend directly to farmers, the Farmers Home Administration is the largest and the most important in terms of reflecting the credit policies and structural interest of the Department of Agriculture. In 1981, the Farmers Home Administration's portfolio was nearly 50 times its size in 1960, with more than $14 billion in grants and loan obligations extended in 1979 alone. In approximately 6 years, the Farmers Home Administration's share of total farm indebtedness has risen from 4 to 14 percent.

Any Federal credit activity involves some degree of subsidy. In essence, a subsidy is granted when a borrower obtains funds at an interest rate lower than would have been paid for a comparable private loan. A study by the Federal Reserve Board indicates that this kind of subsidy amounted to about $24 billion in 1980.

The Federal Government "crowds out" private borrowers in two significant ways. Much public attention has been focused on direct Federal borrowing for financing budget deficits. Less well known is the growth in private sector loans that are guaranteed by the Government. Guaranteed loans rose from over $45 billion in 1978, to over $60 billion in 1979, to nearly $69 billion in 1980, to more than $90 billion in 1981.

The continuing high and volatile levels of interest rates are, of course, at the heart of the present economic difficulties. Banks are

extending their resources to carry existing borrowers somewhat beyond the limits of credit worthiness. In a recent report to Congress prepared jointly by the Small Business Administration and the Federal banking agencies, over 75 percent of small businesses surveyed indicated considerable satisfaction with their banks' efforts to assist them with financing. It appears that most banks have engaged in loan renegotiation, interest-only payment plans, extension of loan maturities, and even significant rate reductions to assist struggling small business and farm borrowers through the current difficult period.

Most public comment on high interest rates has emphasized that the Federal Reserve Board, in maintaining a "tight money" policy aimed at reducing inflation also reduces the supply of credit available to borrowers—thereby raising interest rates. What is rarely pointed out, however, is that the Federal Government is also exerting tremendous influence of the demand side of credit markets. The use of Federal credit programs—loans and guaranteed loans—has doubled in the past 4 years, from $71.6 billion in 1977 to an estimated $147.3 billion in 1981, and during the same period the Nation has experienced record-high interest rates. Even though strong pressures are being exerted for the growth to continue, the President has indicated that forceful actions will be taken to restrain Government loan growth during the 1982 fiscal year.

Madam Chairman, borrowed funds to finance expanded output and rising costs have become the lifeblood of modern agriculture. The Agricultural Bankers Division of the ABA conducted a survey to assess the financial conditions of farm borrowers. Results of the survey show that in comparison to that of 1980, the current anticipated situation for funds availability at banks is good. Current demand is somewhat lower than a year ago partly because of more careful financial planning, general uncertainty of the economy, and high short-term interest rate levels.

Some of our other findings are as follows:

One, year end 1981 financial statements show expected declines in net worth and deterioration in financial ratios.

Two, the primary limiting factor on use of credit in 1982 will be the debt servicing ability of farmers.

Three, farm loan delinquencies and defaults are higher than normal, and higher than one likes, but currently do not reflect a crisis condition. However, should high interest rates and low commodity prices continue through the 1982 crop year, a number of farmers will no longer be able to manage their debts and they will find it necessary to dispose of some of their assets.

In summary, the deteriorated financial condition of farmers is primarily due to low livestock and crop prices, high interest rates and high operating costs. This has been accompanied by a general decrease in value of inventories and capital items resulting in a decline in farmers' net worth.

The solution to the farm economy is not more loans. The solution is low interest rates. The solution is higher commodity prices. The solution is lower production costs. The solution is improved income, not more loans.

Additional authorizations for the Farmers Home Administration should be primarily through the guaranteed programs allowing pri-

vate lenders to make loans within reasonable time periods at market interest rates. The Farmers Home Administration direct loan program should be "stretched" through the use of subordinated collateral arrangements in coordination with private lenders.

The ABA supports the administration's basic philosophy of a reduced budget for Farmers Home Administration programs. The economic emergency and business and industry lending programs of the Farmers Home Administration have been singled out for Federal funds reduction and eventual elimination. As a result, the Farmers Home Administration will have to narrow its focus to those borrowers who lack access to other credit sources and not serve as a source of below-market interest rate loans and loan guarantees to a wide variety of private creditworthy borrowers, as it has in the recent past.

Thank you, Madam Chairman, and I will try to respond to questions from you and other members of the committee. I would also like to say that a written statement has been submitted by me, and I would like to ask that this oral statement also be included as part of the record.

Thank you.

Senator HAWKINS. It will be. All statements will be part of the record and there will be statements and questions submitted by other committee members. I have a letter from Senator Quayle on the subject.[1]

[The following letter from Senator Quayle was received by the subcommittee:]

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COMMITTEES:
ARMED SERVICES
BUDGET
LABOR AND HUMAN RESOURCES

April 20, 1982

The Honorable Paula Hawkins
Chairman
Subcommittee on Agricultural Credit
and Rural Electrification
1327 Dirksen
Washington, D.C. 20510

Dear Paula:

Thank you for extending me the opportunity to comment on the reauthorization of the Farmers Home Administration (FHA). FHA has played an important role in maintaining a vigorous and stable farm economy for over forty years. I believe periodic review such as your subcommittee is performing is vital to assure that FHA continues to fulfill its original goals in the ever-changing American farm economy.

I believe that the primary objective of FHA credit programs should be to assist our younger farmers desiring to establish farming operations and to serve as a lender of last resort in assisting established farmers whose operations are threatened by natural disasters or unusually adverse economic conditions.

Modern farming in America is the most efficient and productive in the world. The great productivity of our farmers is the result of intensive use of modern hybrid seeds, fertilizers, breeding stock, and machinery. The corollary of productivity is a rather sizable investment on the part of farm operators who wish to remain competitive. In addition, the price of land skyrocketed in the 1970s. Because of the great increase in the cost of farming in the past fifteen years, it has become extremely difficult for young people to raise the capital needed to get started in farming. I believe, therefore, that FHA can continue to play a useful role in helping young people to start farming careers. We need to continue to attract dedicated and hard-working young people into farming. FHA should continue to make an investment in the future soundness of the farm economy by helping young people with the capital that they cannot acquire from other sources.

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FHA also plays an important role in providing short-term credit assistance to established farmers affected by economic or weather-related problems beyond their control. In recent years, inflation has raised the cost of farming dramatically, and many farmers have incurred substantial debt loads. A decline in prices received by farmers, such as we have seen the past few years, can threaten the life-long investment of even the best-managed farm. In such circumstances, the availability of short-term credit assistance from FHA can contribute to protecting the life-long investment of individual farmers and the long-term stability of the farm economy.

I also believe that FHA should conduct its lending activities in a way to protect the interests of the U.S. Treasury, and ultimately the taxpayers. I welcome the increased emphasis of the Reagan Administration on crop insurance as a protection against weather-related disasters. Additionally, the FHA should, as any other lending institution, assure that prudent lending practices are followed in its credit programs. I do not believe there is any inconsistency between the objectives of FHA credit programs and prudent lending practices.

Although I do not wish to comment on specific FHA programs at this time, I would like to emphasize my conviction that FHA should focus its credit programs on the objectives I have outlined above. Too often in the past FHA has issued loans for persons or projects only peripherally related to farming. While we must pay attention to economic development in rural areas, I believe the primary goal of FHA must be concentrated on farming itself. Additionally, I believe that FHA must be more discriminating than it has been in the past in directing its credit assistance to those who need it to get started or to protect their hard-earned investments. FHA credit should not be used to expand successful operations or to prop up badly-managed operations. Extension of credit by FHA for purposes such as this have only served to add to inflation in the price of farmland and to expand the already over-extended credit budget of the Federal government. In many ways the over-extension of credit by FHA has contributed to inflation in the farm economy, and this inflation is partly responsible for the current earnings crisis of farmers.

Finally, I would like to call your attention to certain problems in the administration and delivery of services under the FHA credit programs. During the past year there has been an unusually heavy demand for FHA loans in Indiana because of adverse weather over the past 18 months. The local FHA offices in Indiana have

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been unable to process either the emergency disaster loan applications or the normal load of operating loan applications in a timely manner. Since farming is a seasonal business, delays in receiving credit can cause exceptional hardship for recipients.

I believe FHA should take appropriate measures to assure that its credit assistance can be delivered in a reasonable and appropriate period of time. This may require increased advance planning to assure that enough personnel are assigned to local offices to meet demand. Since great attention and prudence must be used in evaluating each loan application, I believe it is imperative that enough properly trained and experienced personnel are available to handle loan applications. In addition, I believe we should evaluate the application forms used in FHA credit programs. Complex and redundant application forms can also contribute to delays in processing. Again, I believe that we should follow the principle of assuring the timely delivery of credit in a financially prudent manner.

I welcome this opportunity to comment on the reauthorization of FHA. I look forward to working with you in the future, and commend you for your leadership in finding responsible ways to continue the FHA and adapt its programs to the current economic and fiscal circumstances.

Sincerely,

Dan Quayle
U.S. Senator

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Senator HAWKINS. I welcome Mr. Sacia, legislative assistant to the National Farmers Union. Do you have a statement?

Mr. SACIA. Yes, I do.

Senator HAWKINS. Please proceed.

## STATEMENT OF PAUL SACIA, LEGISLATIVE ASSISTANT, NATIONAL FARMERS UNION

Mr. SACIA. Thank you, Madam Chairperson.

I am Paul Sacia, legislative assistant for the National Farmers Union.

When we testified on the reauthorization of Farmers Home Administration, and the applicable loan ceilings for fiscal years 1983 through 1985, before the House subcommittee early last February, we projected that a doubling of the administration's proposed levels would be needed.

At that time, we proposed that $4 billion in FmHA farm ownership and farm operating loans funds be authorized for fiscal year 1983, together with releasing the $600 million in economic emergency loan programs authorized in the Agriculture and Food Act of 1981, and extension of that program with another $4 billion in loan authority.

Since that time, conditions have become appreciably worse and the levels which we advocated in February may not be sufficient.

Frankly, we were appalled at the suggestion of Farmers Home Administration and USDA officials last Thursday that the administration's recommended levels would constitute "ample provision to provide a last resource source of credit to family farmers."

Such assumptions must contemplate the attrition of perhaps 100,000 or more farmers now in desperate difficulty, through no fault of their own, but principally because of the combination of high interest rate and low farm income.

The Farmers Home Administration is not meeting today's credit needs of farmers and will not be able to do so under the recommendations made to this committee last week.

At this time, I would like to commend Senator Jepsen for his statement last week.

The recommendations of the recent 80th national convention of the Farmers Union here in Washington, D.C., are indicated in attachment A.[1]

The members of this subcommittee undoubtedly are aware of the great volume of evidence of the magnitude of the agricultural credit crisis. Much has recently been reported by authoritative reporters in the spoken and printed media.

What we are hearing when we go out in the country is in total contradiction of what we hear from USDA. As an example, in 1981, the Department told us that there were 300 foreclosures. We know there are 304 farm mortgage foreclosures in the State of Minnesota alone in 1980. The situation has worsened greatly since that time. Also, we were able to obtain a fact sheet from USDA, which is attachment 1 to our statement, which show there are over 2,300 farm

[1] See p. 119 for attachments A–F to the statement of Mr. Sacia.

foreclosures— mortgage foreclosures for the year ended November 1, 1981.

Also, in that same statement, it shows an additional 1,270 bankruptcies, plus for the month of November alone there were 409 voluntary liquidations and reportedly 291 involuntary liquidations which will be recorded in the near future for that month. That concerns us.

We are also concerned that the farm foreclosure figure is not the tally we should necessarily be looking at if we want some measure of the severity of the farm crisis right now. We think we should be looking at such figures as bankruptcies, involuntary liquidations, voluntary liquidations, notice of acceleration of demand for payments, and letters sent to farmers asking them to consider quitting farming. All of those things should be taken into consideration when measuring Farmers Home Administration procedures and perhaps on their delinquency rate.

Recently, National Farmers Union conducted a series of nine regional factfinding hearings. On a number of occasions at these hearings, rural bankers presented testimony which indicated that many farm operators are just hanging by a thread as they face this year's production season.

Attachments B, C, D, and E present some of these presentations by working bankers in rural America.

Attachment F is a portion of our House subcommittee statement which focuses on, one, the severity of the present agricultural economic crisis, and, two, our consternation with the USDA's refusal to acknowledge the dire predicament in which many American farmers find themselves.

Finally, I would like to mention that we believe that this situation is not a survival of the fittest phenomenon. We have had 3 bad years in a row. The farm income rate and the prices that farmers are receiving, 57 percent of parity, are the lowest since 1933. The farmers that are going to be squeezed out are the youngest, are the best educated, some of our very best farmers. And we believe that to allow this to happen, to not make the investment now, is to deny vital agriculture in the future.

Thank you very much for your time.

Senator HAWKINS. Thank you for participating today.

Mr. Miller, I have questions for all of you at length.

I would note that the primary threat to the income of farmers come from natural disasters and low prices. The Government has addressed the problem by creating a crop insurance program and by continuing the emergency disaster loan program.

Since low prices can also jeopardize farmers' net income, I have become interested in finding ways to safeguard a reasonable return to the farmer and at the same time insure the taxpayers from loan defaults.

We might be able to do this by encouraging borrowers to lock in a safe price on the futures market, or better yet, with agricultural options when they become available.

Do you view taking steps to protect farmer income as a positive endeavor?

Mr. MILLER. Madam Chairman, we certainly do. I think the recommendations which you outlined prior to the hearing and possi-

bly using the issue of options as one measure to protect a certain level of that income are commendable. I do, however, think that they will reach a limit where they will not be completely effective if it gets to the point where that is the only measure that a farmer has to secure himself against a possible default.

What I am saying, up to this point, by and large, what has kept farmers in business over the years and made it at least marginally profitable over the long term has generally been the increased value of the land that they farm. Owning farmland was about the only way that a farmer could stay in business.

I hope that this committee is successful in developing several recommendations, and our organization certainly favors the use of options on an experimental basis to the point where we can determine how effective they are going to be. But I certainly think it is time for some innovation and we are encouraged about the type of fresh thinking and new approaches that have been discussed already.

Senator HAWKINS. Do you have any ideas of your own that would better the future of the farmer?

Mr. MILLER. We have an idea that lower interest rates would help a lot.

Senator HAWKINS. Farmers, businessmen, and housewives.

Mr. MILLER. I certainly agree with you. I think farmers are not in the situation all by themselves. And there is no question but what all segments of the economy are being affected. One thing that does concern us, however, is the effect that high interest rates are having on the related industries of agriculture and turnaround in farm prices is going to be absolutely necessary.

We would like to see the administration make the reduced acreage program more attractive through either raising the loan rates on TCC or regular and reserve loans, or do any other measure that is going to secure that those farmers who have signed up in the reduced acreage program will actually go through and participate; they will reduce their planting. The sign-up rates are very encouraging, but we are bothered that possibly they will not participate, go all the way through the program. And there is just no way we are going to raise general farm prices unless we get the price of grain up. And in order to do that it appears there is going to have to be a smaller crop.

Senator HAWKINS. Farmers Home Administration said that policy should emphasize the servicing of loans to help farmers graduate to private lender credit. Do you think Farmers Home is doing a good job helping graduate borrowers out of FmHA?

Mr. MILLER. We are encouraged at the direction that we see in recent months, encouraging farmers to graduate to other sources. I think in the past there has been some reticence on the part of the local committees to encourage that for a number of reasons. And I think the outstanding loan portfolio is something that Farmers Home Administration officials keep their eye on. I think they use that as a barometer, an indication of how successful they are in encouraging Farmers Home Administration in borrowing.

I certainly believe that it is a wise policy and it is certainly a policy that our organization supports.

Senator HAWKINS. In your statement, you pointed out that there is adequate credit available for farming, but later on you say that farmers are running out of unencumbered assets to borrow. Last week, the Farmers Credit Administration testified before this committee that the debt-to-asset ratio for the farm community in the United States is 1 to 4. Can you explain to the subcommittee how it is possible for an industry with such an enviable equity picture to be running out of unencumbered assets to borrow against?

Mr. MILLER. I think probably that the first thing that needs to be explained is that the possibility that farmland values will not retain their current value that they have right now. It is certainly something that bothers us a lot. It appears that it is occurring in a spotty form right now. There are parts of the country where land values are decreasing and there are other parts where they are pretty much holding their own.

I think farmers are generally wise managers and they are afraid to borrow 100 percent of their available limit. And that 1 to 4 debt-to-equity ratio, I certainly would submit that it is not across the board. That may, in fact, be a gross average. But we are certainly aware of certain farmers in certain parts of the country, particularly it's a very spotty issue, but there are certain parts of the country where there just are not any more assets to borrow against. And, in addition, the cash flow problem, we can borrow and borrow, but if you cannot pay it back then you know what street you are on.

Senator HAWKINS. The administration has stated repeatedly in their fiscal year 1983 budget documents and on this legislation that their primary objective is to return Farmers Home to its traditional role of "lender of the last resort" in the farm community.

What steps would you recommend the agency take to bring its programs into line with this goal?

Mr. MILLER. I think reinstatement of the limited resource programs would go a long way to that effect. I think when it is stated that the limited resource application has not been effective, I believe it is probably based on the fact there are so many farmers out there with low incomes right now that surely Farmers Home Administration is lending a lot of its money, far more than 25 percent, to low income borrowers. But these are not normal times. I think when normal times return and, hopefully, that is very, very soon, that it will be necessary to maintain the limited resource programs in order to effectively maintain in the minds of Farmers Home Administration officials what their mission is, and that is lender of last resort.

We are not advocating and we will not advocate that Farmers Home Administration be in direct competition with commercial sources. The lender of last resort is certainly appropriate and it is certainly something that we support.

Senator HAWKINS. Your organization has observed the activities of FmHA over a long period of time. Have you any observations regarding procedures under which loan activities of the agency are administered?

Mr. MILLER. We have two issues that we think the Farmers Home Administration must address directly. One of them is the ability of FmHA officials to adequately process and adequately render a decision on a loan in a timely fashion.

We recently polled our State leaders in our Grange States and by far and away the biggest complaint that they registered about Farmers Home Administration's lending practices right now is the interminable time delays that are involved in getting a decision out of Farmers Home one way or another. And in farming, as probably in most other businesses, timing is critical in many points.

The second thing, and I touched on it during my presentation, is that we need better educated FmHA officials out in the country. They have got to know what an effective farm plan and a workable farm plan is before they can make an intelligent decision on extending credit, rejecting credit, refinancing credit, how to allow a young farmer or a distressed farmer to expand, for instance, in order to improve their cash flow position. These are certainly things that we think are very important.

Senator HAWKINS. Thank you, Mr. Miller.

Senator Pryor has joined us.

## STATEMENT OF HON. DAVID H. PRYOR, A U.S. SENATOR FROM ARKANSAS

Senator PRYOR. Thank you, Senator.

Senator Hawkins, I want to commend you for holding these hearings and, second, I do have a statement that I would like inserted in the record.[1]

I have only one question relative to the specific testimony and it concerns the inability to obtain decisions from the Farmers Home Administration. Do you feel that this is getting better or worse? Do you feel like they are increasing their sensitivity to respond to these questions or do you feel like it is going downhill?

Mr. MILLER. I am encouraged at the idea that the administration has begun the process of emphasizing the farm production loan program over and above the other lending programs. But I am still convinced that there is a certain wave of uncertainty among Farmers Home Administration officials as to whether or not they really should full hog toward farm production and farm ownership loan programs. Whether or not they ought to retain certain employees who are proficient in housing or business and industry loans.

I cannot say that it is getting better. I can only say that the time delays are long right now. And I think with a definitive expression of commitment to farm production that that time delay will rectify itself.

Senator PRYOR. In past years, Farmers Home Administration has made billions of dollars in credit available to farmers who have suffered economic losses due to natural disasters and the administration is now proposing to cap that particular program—the emergency loan program—at $1.54 billion in fiscal year 1983. I would like your opinion, is it wise at this point to cap the disaster assistance program when natural disasters are so unpredictable?

Mr. MILLER. Senator, I am not sure we should cap the program on the basis that disasters are unpredictable. They always have been and they always will be. I do, however, think that it is wise on the part of the administration to reduce the amount of risk that

[1] See p. 96 for the prepared statement of Senator Pryor.

Farmers Home Administration will buffer against a producing farmer.

That farmer has to be accountable for the risks that they take in the production of food and fiber. Yet, at the same time, it is difficult to ask the farmer to assume all the risks, when farm income is so low that it does not justify it. And it does not justify the enormous capital outlays that it takes to go into production agriculture.

Senator PRYOR. When you speak of risks, that also raises the issue of crop insurance. And I would like to ask you if crop insurance today under the present system is able to replace the Farmers Home Administration's natural disaster loan program?

Mr. MILLER. Our members have communicated to us that widely differing opinions on the all risk crop insurance program. Many of our members are saying that they do not feel satisfied that the specified yield is a true reflection of local growing conditions. In other words, they are not satisfied that the all risk crop insurance program can adequately insure the way that this particular farmer operates and the kind of yields that this particular farmer is capable of producing. In addition, they say that if this is all the level that I can get insurance to, then it does not justify the expense involved. In other words, we have a number of producers who are saying that the all risk crop insurance program needs more work. It needs more time and it needs more thought behind the ability of the Federal crop insurance people to adequately buffer and provide the insurance necessary for the widely varying production.

Senator PRYOR. Do you feel that the Farmers Home Administration today truly recognizes the depth of the crisis that we are facing today in American agriculture?

Mr. MILLER. I am not sure that they do, Senator. Our organization has called for release of the $600 million emergency economic reserve and we have been—our request has been countered with the explanation that there is no shortage of capital. We do not dispute that there is any shortage of capital, yet, if you look at the laws, it says that that EE loan program is designed for either situations where there is a shortage of capital and/or times when farmers are under severe cost price squeeze. And if the severe cost price squeeze right now does not adequately express the situation American agriculture is in, we have been misled as well as, I am sure, everyone else has.

Senator PRYOR. I thank you very much for responding.

Senator HAWKINS. Mr. Sacia.

Mr. SACIA. Yes.

Senator HAWKINS. Earlier in the year there was a great deal of concern about Farmers Home Administration's delinquent loans. Some of us in Congress even proposed a moratorium on loan repayment be established. How do you view the question of moratoriums on repayment of Farmers Home loans?

Mr. SACIA. Our administration has come out in support of it. And I should say it is mostly out of we are just kind of throwing up our hands. The situation has gotten so bad that it is difficult to remedy the situation. Right now we have five individual State farmers union——

Senator HAWKINS. What other actions might be possible short of debt forgiveness to help the farm community, in your opinion?

Mr. SACIA. The first step, the $600 million. We view that as a test of how much this administration really is concerned about the economic plight right now. As long as they continue to hold the $600 million, we just cannot believe that they are concerned at all with what is going on out there.

Senator HAWKINS. Do you feel that Farmers Home has a great deal of discretionary authority to reamortize or reschedule or to defer loan payment?

Mr. SACIA. Yes, they have all the authority they need. The problem of reamortization and rescheduling is that once that is done, oftentimes the interest rate that it will then be set at is higher than what it was originally set at. That makes it somewhat prohibitive to take that kind of measure.

Senator HAWKINS. How do you feel that a majority of farmers who have had to borrow from the private sector view a moratorium on repaying Farmers Home program loans?

Mr. SACIA. That is difficult to say. I would think that if they are in the farming business they understand the situation that especially the younger farmers are under. They do not have the equity to operate under. And I am sure they are sympathetic to what they are going through. I would believe that a majority would be for a moratorium.

Senator HAWKINS. Ms. Thatcher, how do you feel about that?

Ms. THATCHER. Well, I would think that people that borrowed from a private source would think it would be pretty unfair that Farmers Home people were receiving a moratorium when they were not able to receive the same thing.

Farm Bureau does not support the moratorium. They not only feel that it would be unfair for people receiving funding from other sources, but, also, for the Farmers Home borrowers who do pay back their loans on time. It would be unfair to them.

Senator HAWKINS. Mr. Miller, would you like to comment?

Mr. MILLER. Our position is that we do not favor a moratorium because, first of all, the Secretary has that authority right now on a case-by-case basis. And, second off, it would either defer principal or interest or both for simply a moratorium on payments themselves across the board, even to those individuals who are capable of sustaining.

Senator HAWKINS. Mr. Eatherly?

Mr. EATHERLY. Madam Chairman, we feel like the moratorium would not be appropriate. It should be a case-by-case method. We feel that lumping together loans would permit abuses. We feel that some could probably repay their obligations but would not repay them in order to take advantage of the moratorium. We feel that a deferral of loan payments or a moratorium would not be an acceptable gesture to other borrowers who find themselves in almost the same type of financial situation. So we think it would be inequitable, to say the least.

Senator HAWKINS. Mr. Sacia, I am sure you carefully considered the funding levels recommended in your statement for Farmers Home programs. Do you think that your higher lending levels will have any adverse budgetary impact on present economic programs?

Mr. SACIA. As I mentioned in my statement, we believe it is a small investment we are going to have to make now and that it

will be very damaging to the President's economic program to let the foundation of American agriculture go down the drain, because we are not going to free up more money. It might seem like a lot right now, but it is a small investment.

Senator HAWKINS. How did you arrive at your recommended spending levels?

Mr. SACIA. Just from what we see. The lack of funds that are available. In many ways it is difficult to quantify. But we believe in order to satisfactorily have loan money for our farmers and some meetings that we have held around the country—we have held nine regional hearings—and it is just a mark we decided to aim at. And it is very difficult to quantify as I am sure OMB would say it is difficult to quantify exactly how much should be available for these programs.

I guess that is the best I can answer that.

Senator HAWKINS. Thank you. Mary Kay, you handled agricultural matters for our friend Senator Jepsen. Do you believe that Congress and the administration have a proper perspective on the problems experienced by farmers across the country?

Ms. THATCHER. I would hope at least Senate Agriculture Committee members would. I think that through some of the surveys that have been done by the bankers and surveys done by Farmers Home, they should have a pretty good idea of both what the agricultural sector is facing right now.

Senator HAWKINS. Is Farmers Home able to adequately service loan applications and provide counseling to the farmers? Certain farmers have indicated FmHA had not been able to carry out its role?

Ms. THATCHER. Senator, I believe some of our members are concerned especially with the counseling aspects, and, as has been mentioned, they are concerned that when they do put in their loan applications it is taking a longer period of time than they wish, but I believe they see that turning up and I think they are encouraged that Farmers Home is working to get that done. We have encouraged Farmers Home several times in communications that they need to work on some of their people out in the field; that once the loan is made they need to keep working with the people and keep up with the review process, and especially on graduation to regular rates.

Senator HAWKINS. Can you tell the subcommittee how many of your members who have FmHA loans are young farmers and how many of them have been farming more than 10 years, and still need Farmers Home protection?

Ms. THATCHER. No; I could not.

Senator HAWKINS. Could you supply that to us?

Ms. THATCHER. I will.

Senator HAWKINS. Thank you.

What are your views on the administration's proposal to eliminate the limited resource loan program?

Ms. THATCHER. We do not support that proposal. While I guess it would be good from a budgetary standpoint, that program has served the beginning farmers very well, and we do not believe that this would be the time to pull the rug out from under it.

Senator HAWKINS. What are your views on targeting the B. & I. loans to areas of extreme poverty?

Ms. THATCHER. We do support eliminating the B. & I. program altogether, but if that cannot be done, we support putting a maximum limit on projects so that so much of the money is not going to big projects and more small projects can be funded.

Senator HAWKINS. Thank you, Mary Kay.

Ms. THATCHER. Thank you, Senator.

Senator PRYOR. Well, I would like, if I could, Senator Hawkins, to return to the subject of the limited resource farm loan program because I do not know if my figures are correct, but I think the average age of a typical American farmer in this country is the late fifties—57 or 58 years of age. And, for the life of me, I cannot see today how a young person, male or female, can become a farmer. I have talked to many bankers throughout the State of Arkansas who are involved in farm loans and they simply will not make loans to a young farmer unless all the collateral is there, which is almost mortgage free, and that is almost an impossibility these days in the present environment. I wonder if the witnesses might comment on the abolition of the limited resources farmer loan program? I think it would be very pertinent to have their comments.

Senator HAWKINS. Mr. Eatherly.

Mr. EATHERLY. I think it is needed. I think the limited resources farm loan program—the bankers have no quarrel with that. Someone needs to help the young farmer. I do not mean it as a joke because it is serious, but they have a saying down our way that the only way you can get into farming today is to either marry it or inherit it. You cannot do it any other way.

Today, the young farmer cannot even pay the interest on his loan, so he must have some kind of help. The average age of a farmer is about 57 years of age. If the country is going to maintain its quality of farmers and see that they keep farming, someone has to do something, but I do not think anyone has the answer to it, Senator. Economically, it will not work today. The numbers just do not fall in line.

Senator PRYOR. Any other comments?

Mr. SACIA. Yes, we have been on the record in the past of being for 25 percent of available loan money for limited resource borrowing, and we still feel that way.

Senator PRYOR. Is the present program, the limited resource farmer loan program at 20 or 25 percent?

Mr. SACIA. It is 20.

Senator PRYOR. You favor supporting it even up to 25 percent; is that correct?

Mr. SACIA. Yes; and for the very reason of availability to younger farmers, age 57 years old right now and getting older. We need that money desperately.

Mr. MILLER. Senator, if I might add, one of the things—we certainly support the limited resource; we support it at 25 percent funding, but, again, I have to hark back on this that the worst thing in the world that could happen to a young farmer would be for him to be able to walk into a Farmers Home Administration office and get easy money and go out and buy a big farm right off the bat. And without effective counseling, without effective guid-

ance out of that Farmers Home Administration office, those kinds of decisions are not in the best interest of that young farmer and they are not in the best interests of long-term agricultural productivity of this country.

Senator PRYOR. But you do feel that the young farmer must have some loan availability?

Mr. MILLER. Certainly, certainly.

Senator PRYOR. And financial capital.

Mr. MILLER. Absolutely. And that limited resource program is another tool in the bag of that Farmers Home Administration office to be able to do a proper job for a beginning farmer; starting out small, lease a good deal of land, rent a good deal of land, probably rent the equipment or any number of things. But that loan officer has to be the one who can exercise that kind of discretion.

Senator PRYOR. Thank you.

Senator HAWKINS. What interest rate should be established for limited resource loans, Mr. Miller?

Mr. MILLER. Simply from—I believe somewhere around half the cost of money for the Government might be a good place to start talking anyway. I just recently checked the figures and, of course, the ownership loans are a good deal lower than the operating loans, but they are subsidized, there is no question about it, and I think properly so. You start at half the cost of money to the Government and see how it goes.

Senator HAWKINS. I have some questions for Mr. Eatherly, and some I will ask and submit the rest for the record, if you do not mind.

Mr. EATHERLY. Right.

Senator HAWKINS. In your statement, you discuss the Federal crop insurance program as a means of alleviating the impact of natural disasters.

Mr. EATHERLY. Yes.

Senator HAWKINS. Do you think it is wise for FmHA borrowers to carry crop insurance?

Mr. EATHERLY. Yes, I do. I think it is wise for all borrowers to carry crop insurance. I think it is a tool and I think it is more of a safety net in case of natural disasters, and I think it is very beneficial. I think the program is in its infancy right now, but give it another year or two and it will really be recognized as being very beneficial.

Senator HAWKINS. What criteria do commercial banks use to classify an agricultural borrower as delinquent?

Mr. EATHERLY. If he is 1 day past due, he is delinquent and the severity of it is determined by how many days he is past due.

Senator PRYOR. He is speaking as a real banker now.

Mr. EATHERLY. Most agricultural bankers—all agricultural bankers—they know their customers. They know what they own; they know what their equity is, and through the last 2 or 3 years they have seen the equity evaporate in their farmland. And I suppose the most concern that bankers have today is the domino effect. If land starts down dramatically and if it starts down because of a few foreclosures, then all land goes down, and all equity evaporates. That is a concern that we have. But we, as agricultural bankers——

Senator HAWKINS. Is it not a trickle down?

Mr. EATHERLY. Pardon?

Senator HAWKINS. Is it not called trickle down?

Mr. EATHERLY. No; it is not called trickle down. It is a flood. We are concerned about those things.

Senator HAWKINS. How do you feel that commercial bankers view the idea of Farmers Home allowing a moratorium on loan repayment?

Mr. EATHERLY. We are opposed to the moratorium. We think it should be a case-by-case method. We cannot see a moratorium imposed on all FmHA loans. We do not think it is fair to the other borrowers, for one thing. And then the other thing is we think there are some FmHA borrowers who can repay their loans but who would not pay it, and who would probably take advantage of the low-interest loan. Some might even go and buy a money market and deal with it.

Senator HAWKINS. How would your borrowers react if Congress were to include provisions giving FmHA power to allow a moratorium?

Mr. EATHERLY. How would I feel about it?

Senator HAWKINS. How would your borrowers feel?

Mr. EATHERLY. Oh, I think the borrowers who have had loans would like it. But I think the rest of the borrowers would not care for it. You must remember that 10 percent of the farm loans are FmHA loans, and 90 percent would probably be opposed to it and 10 percent would be for it.

Senator HAWKINS. What measures would commercial banks take to cooperate with Farmers Home and the Farm Credit System in order to meet the credit problems faced by borrowers this spring?

Mr. EATHERLY. We are working very closely with the Farmers Home Administration. We have worked out deals, they have worked them out with us since they have the Farm Credit System. They will subordinate their position enabling commercial banks to make operating loans, and to keep them in business and to keep them current, so there is teamwork going on now.

Senator HAWKINS. Have commercial lenders seen any FmHA borrowers graduate to private sources?

Mr. EATHERLY. Very few, not enough. It is awfully hard to push a man from a 5-percent rate to a 15-percent rate. It has been difficult.

Senator HAWKINS. Are commercial banks lending to agricultural borrowers at the same level that they did last year?

Mr. EATHERLY. The loan demand is down. It is down for two reasons: Some of our customers have all they could ever pay back and then some do not want to borrow any more money. The loan demand for commercial banks is down at least by 10 to 12 percent.

Senator HAWKINS. Are there sufficient funds to lend?

Mr. EATHERLY. There is an abundance of funds.

Senator HAWKINS. Plenty of money?

Mr. EATHERLY. Yes, Madam.

Senator HAWKINS. How does the level of credit provided by commercial banks compare with the level of credit requests received from borrowers?

Mr. EATHERLY. I am sorry, I did not understand what you said.

Senator HAWKINS. How does the level of credit provided by commercial banks compare with the level of credit requests received from borrowers?

Mr. EATHERLY. Well, there is no problem. The funds are there. There is an abundance of money, and the borrowers are being taken care of.

Senator HAWKINS. Do bankers see encouraging farmers to cut back on certain operations?

Mr. EATHERLY. Yes, Madam Chairman, we certainly are. We are being more than consultants and working very closely with them. One of the biggest problems the farmers have is marketing strategy. They do not do a good job of marketing. We think that if they did, they would be in better shape. We also feel that if we could get our export program going, they would probably be in better position. Those two issues really are of paramount concern to bankers right now.

Senator HAWKINS. The American Bankers Association concluded a study of the financial condition of farm borrowers which indicates that the current and anticipated situation and credibility of banks is good. Why do you think there has been so much media coverage of the proposed lack of credit for farmers, almost every major magazine?

Mr. EATHERLY. The demand for money is not as great as it was last year. The money is there. In tight money times I do not think you would see as much publicity about it, but I think because we have just come off of a high demand, high ratio, and where the loans are not as apparent right now, maybe that is where the publicity is coming from.

Senator HAWKINS. Senator Helms has requested that I ask you this question: The supporters of the B. & I. program have pointed out that Government guarantees are necessary for this program because rural banks do not have sufficient assets to allow them to make the large loans for capital invested in industrial projects. In addition, commercial banks are traditionally short-term lenders and the Federal guarantees make longer term loans possible. In your view, is this an accurate assessment of the rural credit situation for business loans?

Mr. EATHERLY. It is difficult for commercial lenders in the private sector to come into rural America, in a small town and make a large loan. I grant that.

The American Bankers Association has taken the point of view that because of the alarmingly high interest rates, and because of the deficit, that at this time it might be best to support the withdrawal of the B. & I. funds. That it would be inflationary, but it is something maybe we could handle some other way, maybe the private sector and other large commercial banks could come in and help.

Senator HAWKINS. Thank you, Mr. Eatherly.

Thank all of you. We will excuse you at this time and call our next panel.

We will call John Hall, chairman, rural water task force; Bruce Workman, member, board of directors, Winter Haven; and Robert Doyle.

**STATEMENTS OF JOHN HALL, CHAIRMAN, RURAL WATER TASK FORCE, ADEL, IOWA, ACCOMPANIED BY BRUCE WORKMAN, MEMBER, BOARD OF DIRECTORS, WINTER HAVEN, FLA., AND ROBERT DOYLE, LEGAL COUNSEL**

Senator HAWKINS. Welcome, gentlemen.

Mr. HALL. The Water Quality Association appreciates this opportunity to comment on S. 2314, a bill to amend the Consolidated Farm and Rural Development Act to reauthorize the Farmers Home Administration for each of the fiscal years 1982, 1984, and 1985.

Our views this morning relate to the single issue of Government-financed competition with private enterprise. My name is John Hall. I am chairman of the Water Quality Association's rural water task force. I am also president of a franchised water improvement equipment dealership in Adel, Iowa.

With me this morning are Bruce Workman, a member of the association's board of directors, and a water improvement equipment businessman from Winter Haven, Fla., and Robert Doyle of Washington, D.C., counsel to the association.

The Water Quality Association is a nonprofit organization headquartered in the Chicago suburb of Lombard, Ill. It consists of members who are engaged in the manufacture and in the wholesale and retail distribution of water treatment equipment which, at the point of use, improves both raw and municipally treated water in the precise quantity and to that particular quality required for any special or general use, whether in homes, in institutions, in commercial establishments, or in all varieties of manufacturing and other industrial occupations.

Through the technologies, products, and processes of point-of-use treatment, water, whether it is needed as working water or as drinking water, or simply as water usually wasted, is treated to the content quality required for the specific use needed, in the amount actually desired, and at the point utilized. This treatment service is provided by this industry anywhere from a single faucet to a small community, and throughout the entire range in between.

The point-of-use water treatment industry consists of more than 200 manufacturers, about 5,000 retailers/distributors/wholesalers, and does nearly $1 billion in annual sales. This industry employes over 50,000 of our fellow American men and women, it serves in excess of 6 million families and more than 250,000 commercial/industrial/institutional customers. It has the potential for materially assisting governments in assuring water's safety through attainment of goals as well as satisfaction of standards.

Through voluntary membership, some 1,400 members of this industry support the Water Quality Association, the objectives of which are the facilitation of information exchange, the conduct of educational and community affairs programs, the publication of materials relating to the quality of water, and other functions of a traditional trade association nature which are intended to benefit the public through industry betterment.

For the information of committee members, a detailed description of our industry and its products, processes, applications, and potentials is provided in the appendix to this statement.[1]

The point-of-use water treatment industry is capable of, and does fill a need with treatment technologies that exist almost across the whole board and throughout the entire spectrum of possible requirements.

Stated simply, our technology, products, and people can and should be more fully utilized in the attainment of national drinking water goals, in the satisfaction of water needs and standards, in the provision of water supply treated to the quality required by industry, by commercial establishments, by health care and other types of institutions, by other applications on the farm or in the home, and by public and individual needs and desires.

This technology is particularly useful in the smaller rural communities of America, those very communities which have an extremely serious cost problem in meeting Government standards. Pages A–5 through A–7 of the appendix to our statement explains this issue in detail, including some cost comparison figures which persuasively argue in favor of wider utilization of our industry's potential at the rural level.

One of the existing barriers to this greater usage arises out of the direct and destructive competition fostered and promoted by Government-financed rural water districts. The Farmers Home Administration funds this competition, competition with private enterprise, and it does so at low rates and for long terms.

The effects on our association's members are not only harmful to these small businesses, but injure the public as well through the process of displacing utilization of technology which is an alternative water treatment method more preferable in a great many cases to the Government-funded central treatment and long line distribution method.

Last September, working with the staff of Senator Jepsen, we were able to develop some rather revealing and impressive figures to document the seriousness of this issue and its cost to the Government.

These figures, arranged in tabular form, and relating to those rural districts in the single State of Iowa, are as follows:

And we would like to submit these for the record.

Senator HAWKINS. Surely.

Mr. HALL. The first column identifies those rural water districts in Iowa, categorized by organization. The third, fourth and fifth columns indicate the amount of Federal funding involved, broken down by loans and grants per rural water district. The sixth shows the number of users per district and the eighth, the amount of loans per user. The last vertical column indicates the Federal subsidy per user per year, based on the difference, at the time of the figures' compilation, between the cost per user per year. At the amount of interest charged for the loan by the Farmers Home Administration as compared to the 17 percent being charged by the open market.

[1] See p. 129 for the appendix to the statement of the Water Quality Association.

In other words, the Federal Government is not only competing directly with private industry by displacing the small businessman, but it is doing so at rates far below the market and at prices and on terms which no one else can even consider.

This practice, furthermore, amounts to budget deficit aggravation through provision of direct subsidy. The figures clearly illustrate this fact.

In the first horizontal column, for instance, the difference between the 17-percent market rate for interest on the $4,800 loan and Farmers Home Administration rate is $580 per user per year. Multiplied by the number of users in that particular district, the Federal subsidy for that single district in Iowa alone is $471,000 per year. Over the 40 year customary life of such loans, this amounts to almost $19 million. For the 813 users, it totals over $23,000 per individual user. And this example, significantly, only relates to one State, Iowa. It includes only 813 people in a single district. There are other districts, many others.

The last horizontal column, for instance, would compute to more than twice the cost, as over 2,000 users are involved in this district. There are, in addition, many other States as well.

And this assumes that these loans will be repaid. The truth of the matter is that many are not.

[The tables referred to above follow:]

LOANS AND PREAPPLICATIONS/APPLICATIONS 9-2-81

| NAME | ESTIMATED AMOUNT TO BE FUNDED | FmHA AMOUNT FUNDED | LOAN | GRANT | NUMBER OF USERS | AVERAGE GRANT/ USER | AVERAGE LOAN/ USER | ANNUAL INTEREST SUBSIDY/USER @17% MONEY COST |
|---|---|---|---|---|---|---|---|---|
| Rural Water System #1<br>Hospers, Iowa | $ | $ 4,140,200 | $ 3,936,000 | $ 204,200 | 813 | $ 250 | $4841 | $ 580 |
| Lyon & Sioux Rural Water System, Inc.<br>George, Iowa | | 5,471,100 | 5,267,500 | 203,600 | 911 | 223 | 5782 | 694 |
| Cherokee County Rural Water District No. 1<br>Cherokee, Iowa | | 7,320,000 | 5,742,800 | 1,576,200 | 900 | 1751 | 6380 | 785 |
| West Central Iowa Rural Water Association<br>Manning, Iowa | | 7,175,800 | 6,746,800 | 429,000 | 1200 | 357 | 5622 | 675 |
| Rathbun Regional Water Association<br>(including Wayne, Monroe, Lucas,<br>Appanoose, Davis), Centerville, Iowa | | 28,652,300 | 26,395,300 | 2,257,000 | 6400 | 352 | 4124 | 495 |
| Napello Rural Water Association<br>Ottumwa, Iowa | 704,000 | 4,361,800 | 4,315,000 | 46,800 | 1543 | 30 | 2796 | 335 |
| Clarke Rural Water District No. 1<br>Osceola, Iowa | | 174,000 | 174,000 | | 77 | | 2260 | 271 |
| Clearfield Rural Water District, Inc.<br>Clearfield, Iowa | | 170,000 | 201,500 | 91,750 | 52 | 1764 | 3875 | 465 |
| Shelby County Water District No. 1<br>Harlan, Iowa | | 3,380,600 | 2,477,800 | 902,800 | 450 | 2006 | 5506 | 660 |
| Page I Rural Water Association<br>Shenandoah, Iowa | | 6,199,400 | 4,553,000 | 1,646,400 | 1100 | 1497 | 4139 | 497 |
| Mahaska Rural Water System, Inc.<br>Oskaloosa, Iowa | | 6,440,400 | 4,443,400 | 1,997,000 | 960 | 2080 | 4629 | 555 |
| Berwick Water District<br>Berwick, Iowa | | 702,000 | 360,000 | 342,000 | 175 | 1954 | 2057 | 247 |
| Osceola County Rural Water Association<br>Sibley, Iowa | | 20,200,000 | 20,000,000 | 200,000 | 2200 | 91 | 9091 | 1091 |
| Clay County Rural Water Association<br>Spencer, Iowa | $ | $ 9,150,000 | $ 8,150,000 | $1,000,000 | 945 | $1058 | $8624 | $1035 |
| Southern Sioux Rural Water Association<br>Ireton, Iowa | | 6,218,000 | 5,718,000 | 500,000 | 641 | 780 | 8078 | 969 |
| East Dickinson County Rural Water Assn.<br>Spirit Lake, Iowa WITHDRAWN | 5,000,000 | | | | 626 | | | |
| Marion County Rural Water Association<br>Knoxville, Iowa | | 5,330,000 | 5,130,000 | 200,000 | 750 | 267 | 6840 | 821 |
| Warren County Rural Water Association<br>Indianola, Iowa | 4,800,000 | | | — | 800 | | | |
| Jasper County Rural Water Association<br>Newton, Iowa | | 12,449,000 | 10,449,000 | 2,000,000 | 2071 | 966 | 5045 | 605 |
| Poweshiek County Rural Water Association<br>Montezuma, Iowa | 9,700,000 | | | | 1205 | | | |
| Van Buren County; Rural Water Association<br>Keosauqua, Iowa NOT FEASIBLE | 676,000 | | | — | 200 | | | |
| Xenia Rural Water Association<br>Woodward, Iowa | | 3,200,000 | 3,200,000 | — | 800 | | 4000 | 480 |
| Southern Iowa Rural Water Association<br>1. Grand River Source Area<br>2. Lake Icaria Source Area<br>3. Little River Source Area<br>4. Honey Creek Source Area<br>5. White Breast Source Area | <br><br>4,500,000<br>8,300,000<br>3,000,000<br>3,500,000 | 1,475,000 | 1,200,000 | 275,000 | | | | |
| Southeast Polk Rural Water District<br>Des Moines, Iowa | 2,000,000 | | | | | | | |
| Story County Water Association<br>Nevada, Iowa INACTIVE | 9,000,000 | | | — | 1450 | | | |

Mr. WORKMAN. Iowa State has just completed this study on the operational characteristics of rural water systems in five north-central States,[1] which as this study states in part, 70 percent are behind in their repayment schedule and that absolutely none of the 108 districts even had made any provision for depreciation, for replacement of capital items.

For the committee's use, if desired, I can make available at the conclusion of this record this press release that was just issued by Iowa State.[1]

In addition, the U.S. General Accounting Office has conducted a study [2] in an August 1980 report, that made conclusions similar to those in the more recent Iowa State study.

That report also contains an executive agency group conclusion emphasizing the need for utilizing alternative technologies in rural areas.

To get back to the statement, we are talking about a lot of money. This is Federal subsidy money which competes with private enterprise. In these times of budget consciousness, the Congress might well be interested in reviewing it.

It is not as though there is no existing alternative to this practice—not as though these users have no choice other than to accept the Federal subsidy or simply forego water treatment improvement. That is the whole point of our position.

Our industry has developed technology and the products ready to service these needs. We are merely being ignored. Not only that, but no one in this subsidy-provision agency function, to our knowledge, has even considered the desirability of conducting a study of the feasibility of utilizing these alternative treatment techniques in comparison to the traditional central treatment long line distribution method. Not included in the decisional criteria is what in fact may be better or more cost effective.

It is our judgment that the time is overdue for some provision to be made requiring FmHA to investigate, study, and seriously consider benefits in relation to costs; to act so as to maximize efficiency; to explore the existence and utility of all available alternative approaches to its objectives and to adopt the one producing the maximum benefit and minimum cost to society.

We in the point-of-use water treatment industry have been attempting for some years to prevail upon the Government to at least consider alternative technology in this area. Like everyone else, we would like to have consumer financing provided by the Federal Government. But, let there be no misunderstanding, as businessmen we believe in the free enterprise system. We are not seriously asking for a Government handout. The truth of the matter is, we would be content to have the Government simply remove itself as an obstacle to the normal function of free choice and free markets, and let us do the job we are both equipped and ready to do.

Thank you for the opportunity to present these views.

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[1] The Iowa State study referred to above has been retained in the committee files. See p. 138 for reprint of the press release.

[2] The GAO study has been retained in the committee files.

Senator HAWKINS. Thank you for coming. It appears that your industry has a promising future. How has the onsite technology been accepted in the rural communities?

Mr. HALL. Very, very well. We service in my own area approximately 50 percent of the rural community in some type of service.

Senator HAWKINS. Have you met with Farmers Home officials to explain the technology?

Mr. HALL. Several times.

Senator HAWKINS. What was their reception?

Mr. HALL. Their reception was twofold: One, the reception was cordial. The reply was twofold: Simply, they are only equipped to loan as a lender of last resort. Obviously, many, many individual people that are receiving benefits from the long-pipe solution could not qualify under that lender of last resort provision.

We have talked with them about doing a study on alternative technologies. No. 1, they say they have no funds available for this. No. 2, they felt they might embarrass good people.

We asked them to make studies of three existing districts for cost comparisons.

Senator HAWKINS. Do you provide the full services that rural water districts provide?

Mr. HALL. Well, in answer to that, what, essentially, has happened is that most of the rural water districts are not going into the desert. They are going into places where there has been water. And in most cases, they have had water for 100 years. Not that this water does not have some quality problems. However, their only solution is not to correct those problems, but to replace that water with a long-pipe supply, and that is where we get into the grants needed of $5,000, $6,000, $8,000, and $10,000 per user to run the long pipe.

Senator HAWKINS. Can you meet all the Federal, State, and local health and sanitary conditions?

Mr. HALL. Without a doubt. We do.

Senator HAWKINS. The subsidy figures that you testified to are astonishing. At what rate could your technology provide the same service?

Mr. HALL. Probably—we really have not done a study, but I can tell you, from a practical standpoint, that the average customer that I have probably pays $150 per year total for the treatment of his water, as an average.

Senator HAWKINS. I understand GAO—General Accounting Office—has recently reviewed the point-of-use technology. What was their recommendation?

Mr. HALL. They felt—Bob, would you?

Mr. DOYLE. We can submit this, Senator, for the record. They made a couple of points in here which are rather decisive. First of all, that the rate being charged is not adequate to provide for operation and maintenance as well as capital cost replacement. And another section of the report also deals with a White House initiative that was established a year or two ago consisting of half a dozen Government agencies, the first conclusion of which was that this function of the Government needs to emphasize alternative and innovative technologies in rural areas, which is exactly what we are saying. I have an extra copy, if you would like one.

Senator HAWKINS. Yes. Thank you so much. We appreciate you gentlemen coming today. Thank you so much.

At this time we will call the next panel on rural water/sewer reform. Harvey Johnson, Mississippi Institute for Small Towns; Holly Leach, Water Resources Assistance Corp.; Norman DeWeaver, Center for Community Change; and Ken Bruzelius, midwest assistance program.

Do you have statements you would like to put on in the record?

## STATEMENT OF NORMAN DeWEAVER, CENTER FOR COMMUNITY CHANGE

Mr. DEWEAVER. Thank you, Madam Chairman. It is a real privilege and pleasure to appear before the committee today.

I would like to introduce my colleagues and associates: Ms. Holly Leach from the Big Sandy Area Development District in Prestonsburg, Ky., and the Water Resources Assistance Corp., who has been working for a number of years helping communities in eastern Kentucky with water and waste water problems. Mr. Harvey Johnson, who is the executive director of the Mississippi Institute for Small Towns, who has worked with communities in that State facing very severe problems in the water and waste water areas. And Mr. Ken Bruzelius, who is the executive director of the midwest assistance program, who runs a technical assistance organization that works with rural communities throughout the Great Plains States.

We have a prepared statement, Madam Chairman, which we would like to submit for the record.[1] If I may, I would just summarize briefly some of the highlights in the statement.

First of all, we think your approach, as indicated in your opening statement, Senator, is an extremely positive one. We totally agree with your premise that the available resources in the Farmers Home Administration programs should, in fact, be devoted to communities that are too small or too poor to be able to meet their essential human needs for water and waste water services. And it is that premise that underlies all of the recommendations that we would bring to the committee.

We feel that the Farmers Home Administration system, is currently under severe stress. It is under stress because of the fact that several things have happened over the last several years to which the system has not really accommodated itself.

The resources available to the programs have been severely reduced. At the same time, the interest rates of the loan programs, which is the basic assistance mechanism, has been drastically increased. As a result, changes are needed in the program to make it workable for rural communities.

The Agriculture Committee of the Senate as well as its counterpart in the House understood that changes were necessary. And in your recommendations in the conference committee report on the Reconciliation Act and the farm bill, you suggested a number of adjustments which Farmers Home should make to make the program workable.

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[1] See p. 139 for the prepared statement of Mr. DeWeaver.

Unfortunately, Farmers Home Administration has not implemented those recommendations. What we are suggesting today is that you take legislative action to put those recommendations into force.

We are particularly interested in five key issues as are outlined in our prepared statement. One has to do with the interest rate. The Farmers Home Administration, as you know, has increased the interest rate from 5 percent for all communities, which is what it was before the Reconciliation Act took effect, to 12 percent now for nearly all communities and 5 percent for a very small number.

Instead, we favor the position which was taken in the conference committee report on the farm bill which suggests that the interest rate should be 5 percent for communities whose income level is at or below 80 percent of the statewide nonmetro median family income and that there should be graduated rates above that, including a rate of not to exceed 7 percent for communities whose median family income does not exceed 100 percent of the statewide median.

Progression in the interest rate would enable the targeting of assistance and would enable an even progression from one rate to the other rather than the current situation where you get either 5-percent money or 12-percent money.

Second, we favor a change—in a sense, a kind of deregulation—with respect to the grant rate formula. Farmers Home currently uses a very confusing set of rules with respect to the determination of grant assistance for individual projects.

We favor a simple, understandable, predictable formula which would have in it just the two basic factors that relate to the need for assistance: community income level and community size. This would replace the current rules which are interpreted differently in different State offices, and are very difficult for communities to understand.

A centerpiece of our proposal is a project selection system. Again, this is a recommendation which was made in the conference committee reports on the farm bill and the reconciliation bill. This would be a simple, direct priority-setting device to determine which communities get loans and which ones do not, and avoid a situation which my associates will speak to where communities can be held in abeyance with pending projects forever.

We also favor two other recommendations which we believe would help to introduce cost effectiveness into the system. One, to authorize a small technical assistance program for the small rural communities to have some way to receive disinterested advice in terms of how to solve their problems and also a predevelopment fund approach which would enable those communities with very serious technical problems to explore them so that they could, in fact, have access to the system rather than being frozen out of it because they are not sure what the best solution would be to their problems.

We feel that these recommendations go together; that it is a mistake to simply change one aspect of the program, which is the interest rate, because of the way the current rules are tied together which causes unexpected changes in other aspects of the program.

We were very encouraged that your counterpart subcommittee in the House has taken these five recommendations and incorporated those recommendations unanimously, on a bipartisan basis in the pending Farmers Home reauthorization bill. We would encourage you to do so in your deliberations in the Senate.

I would be very happy to respond to questions, but would give my associates, if I may, Madam Chairman, time to speak directly to local problems.

Ms. Leach.

## STATEMENT OF HOLLY LEACH, WATER RESOURCES ASSISTANCE CORP.

Ms. LEACH. Senator Hawkins, I appreciate the opportunity to speak to you today.

I am Holly Leach. I am a staff member of the Big Sandy Area Development District, located in Prestonsburg, Ky. My district, comprised of five counties in the east Kentucky coalfields, concentrates its activities on management and technical assistance to local units of government. Together with the Water Resources Assistance Corp., a local nonprofit utility management group, which is an affiliate of the national demonstration water project, I work directly with the region's water and wastewater systems.

Today I am appealing to you on behalf of the citizens and officials of two small communities with whom I have worked closely: Elkhorn City and Wheelwright, Ky. These two communities are typical Kentucky towns, and the hardships imposed on them by the new Farmers Home Administration interest rate regulations are typical.

I would like to insert that having a problem with the Farmers Home Administration is a relatively new experience for us in eastern Kentucky. Farmers Home Administration staff dedication and concern for small low-income communities has been a hallmark of the agency in our region.

Elkhorn City and Wheelwright are rural isolated communities: Elkhorn City, located in Pike County, Ky., has a population of 1,164 persons. Wheelwright, located in neighboring Floyd County, has a population of 892 persons.

The Elkhorn City water treatment plant and distribution system was constructed in the early 1950's, and has had no major modifications since that time. The city presently has an indebtedness of $366,000 as a result of construction of a wastewater treatment plant and collection system, and is current on this obligation.

An application was first submitted to Farmers Home Administration in 1978 to renovate the water treatment plant and extend the system. By October, 1981, this project had achieved first ranking in a regional priority system. However, by that time, Farmers Home Administration had notified local officials that the $392,000 loan required for the project would cost the town 11¾ percent interest. This increase in interest payments would have pushed the minimum bill of $10 for 2,000 gallons of water to $26 for the same 2,000 gallons. Needless to say, the city officials could do nothing but turn down the Farmers Home Administration loan/grant and thus today the much needed renovations are indefinitely postponed

and prospects even more remote, for since that time the Farmers Home Administration interest rate has climbed almost a full percentage point to 12⅜ percent.

Without this project, the supply of water to the residents of Elkhorn City continues to be of marginal quality. And the 94 homes in a neighboring community will not be able to connect onto the renovated system, but rather continue to rely on well supplies which because of housing density are becoming increasingly contaminated.

The community of Wheelwright was built by a succession of several northern steel and coal companies in the early part of this century. The properties and public facilities in the town were well maintained until 1966, when they were acquired by an out of state holding company and allowed to deteriorate for tax purposes. Through a unique cooperative venture, the Kentucky Housing Corp. acquired all real estate from these absentee landlords in September 1979, and with HUD assistance began a massive renovation of the housing stock.

The town was given ownership of and responsibility for the public facilities. The natural gas system posed the most immediate problem. To date, the natural gas system has been renovated, with an incurred indebtedness of $344,509 at 5⅛ percent interest.

Their water system is dilapidated. Constructed in the early forties, it is characterized by daily repairs on major transmission mains, periodic citations for structural hazards at the water treatment plant and a leaking unmetered distribution system. By schedule, the community was to have begun work on the water system, utilizing a Farmers Home Administration 5-percent loan/grant in October 1981.

The higher interest rate which became effective this last October has stopped the proposed and critically needed renovation project, and has dampened the spirit of community leaders. Like Elkhorn City, the Wheelwright project would also enable the town to expand its system into a neighboring community of 122 families. This neighboring community too must wait.

As you see, without a Farmers Home Administration loan at a reasonable rate, these communities and many, many others will not be able to make the needed improvements to their respective water systems. Both have existing indebtedness, and they are current on their indebtedness, and do acknowledge their responsibility to incur increased indebtedness for the betterment of their towns.

The postponement of these needed projects, together with the escalating costs of labor, electricity, chemicals, and supplies are forcing these towns into a totally unreasonable position; namely, to drastically increase user rates on systems not capable of supplying safe drinking water. The inequity of this situation is felt by all, but especially by those on low fixed incomes.

Senators, it is my considered opinion, shared by many, that in this country, and especially in my region, which is so heavily impacted by our Nation's energy needs, safe clean drinking water must be recognized as a right based on necessity not privilege. Unless the interest rates currently being charged by the Farmers Home Administration are lowered, a decent supply of water will simply not be available to the residents of Elkhorn City, Wheel-

wright, and other rural communities in Kentucky and across the Nation.

I would like to conclude by saying the proposed regulations by Farmers Home will not enable these communities to renovate or establish water systems.

With this in mind, we in the Big Sandy district support the legislative changes as outlined in Mr. DeWeaver's testimony.

I would also like to ask that the enclosed by Mayor Ferguson of Wheelwright be made a part of the hearing record. It is a letter addressed to Farmers Home turning down the 11¾-percent loan/grant.

Senator HAWKINS. That will become part of the record.

[The following letter was received by the committee:]

CITY OF WHEELWRIGHT,
*Wheelwright, Ky., February 26, 1982.*

DEPARTMENT OF AGRICULTURE,
*District Director, Farmers Home Administration,*
*Hazard, Ky.*

GENTLEMEN: We wish to express our gratitude for being placed in the Group I Category for a water grant. We would certainly like to take advantage of this opportunity to install a new water system; but at this time, it is not economically feasible for us to undertake this project.

If in the future, interest rates should come down; we would again like to be considered for a grant. We hope you can understand that we are a small community with persons living on very small and fixed incomes. There is no way they could afford to pay exorbitant water bills.

We would like to thank you once again for considering us in this matter, and hope you will keep us in mind in the future.

Respectfully,

ELMER FERGUSON, *Mayor.*

Mr. DEWEAVER. Mr. Johnson.

## STATEMENT OF HARVEY JOHNSON, MISSISSIPPI INSTITUTE FOR SMALL TOWNS

Mr. JOHNSON. Thank you. Madam Chairman, I am Harvey Johnson, Jr., executive director of the Mississippi Institute for Small Towns, located in Jackson, Miss.

MIST is a private, nonprofit organization that provides technical assistance to small Mississippi communities in their development efforts. I am also immediate past president of national demonstration water project, a coast to coast network of community-based organizations engaged in assisting rural communities in obtaining improved water supply and wastewater disposal services.

By most standards, Mississippi is the poorest State in the Nation. This distinction has far-reaching implications in the process of increasing the quality of life enjoyed by Mississippi residents. Not only do many communities in my home State lack the infrastructure—that is, primarily adequate water and sewer systems—to support development activities that could lead to better living conditions, but they also lack the local resources to provide this prerequisite of effective community development.

In the past, Mississippi communities have relied heavily upon Federal agencies, particularly the Farmers Home Administration, to provide financial assistance in the development and/or upgrading of their water and wastewater disposal systems. Now it appears that proposed changes in the FmHA water and waste disposal loan

and grant regulations will deny many of these resource poor communities access to a heretofore affordable financing mechanism.

I am, therefore, before you today to express my concern over the possible enactment of these changes as well as to express my support of legislative action that would reinforce the administration's commitment to make the resources of this program available to the smallest and poorest communities.

The specifics of this legislative action have already been detailed by Mr. DeWeaver in his testimony. However, there are several changes recommended by Mr. DeWeaver that I would like to highlight at this time.

When comparing the interest rate provisions of the proposed FmHA regulations with those of the proposed legislative changes, it is apparent that legislative action would be more preferable to small communities in Mississippi than the proposed regulatory action.

For example, under the proposed regulations, about 11 counties in Mississippi would qualify to receive loans at 5 percent while about 16 counties would qualify for the 5-percent interest rate under proposed legislative action. Moreover, an additional 26 counties would quality for 7-percent interest rate loans under the graduated set of interest rates referred to in earlier testimony. However, only seven counties would qualify to receive loans at the intermediate rate, currently around 9 percent, proposed in FmHA regulation changes.

Another key provision of the proposed legislative activities is the establishment of a project selection system. Absent an open and accountable selection system that targets funds to the neediest communities, FmHA funding decisions will continue to be made in an informal and subjective manner. The present process keeps the applicants in the dark and does not provide any assurances that funds are targeted to the neediest communities.

Let us consider the submission and review process that the Glendora preapplication recently went through. Glendora, a poverty stricken town of approximately 220 residents, located in the Mississippi Delta, contacted Farmers Home shortly after receiving a grant from the Environmental Protection Agency to cover approximately 75 percent of the cost of constructing the town's initial sanitary sewer system. FmHA funds are needed to cover the remaining construction costs and are central to the initiation of the project since no other affordable means of financing is available to the town.

Town officials were initially discouraged by FmHA from submitting a preapplication because of the prospect of the unavailability of funds. But the town, nevertheless, submitted a preapplication. It was then implied that the preapplication could not be reviewed because it appeared that Glendora would not qualify for a 5-percent loan and that it could not afford a loan at the market rate.

After the town insisted on a review, the district office informed the town, this time in writing, that a favorable recommendation could not be given until an overdue annual audit and management report had been submitted.

Once the required audit and management report had been submitted and the FmHA district office still had not responded in

writing to the preapplication, the mayor made a written request to the district office that a formal review of the preapplication take place and that the town be provided with a written response.

Finally, approximately 5 months after it was submitted, the district office informed the town, in writing again, that its review of the preapplication had been completed and that the preapplication was being forwarded to the FmHA State office for further processing.

Now, over 6 months after submitting a preapplication for FmHA financial assistance, Glendora is still awaiting a funding decision from Farmers Home.

Under ordinary circumstances, this timetable would appear to be unacceptable, given the fact that raw sewage is running in open ditches and 85 percent of the town's population is below the poverty level. But the Glendora situation is further aggravated by the possibility of losing EPA funding if funding for the entire project is not obtained.

An open and fair project selection system would allow FmHA, the only Federal agency with a long history of service to the smallest and poorest Mississippi communities, to select recipients of loan and grant program resources in a more expeditious manner and based on established priorities.

Another provision of proposed legislative changes in the loan and grant program that would be of particular benefit to small towns in Mississippi is that of authorizing a technical assistance program. Mississippi is a State that is composed primarily of small towns. Of approximately 290 municipalities, over 50 percent have populations of less than 1,000, while only 9 have populations of over 25,000. Moreover, approximately 20 percent of Mississippi municipalities, all with populations of less than 1,000, do not have waste water disposal systems.

Many of these communities not only lack the resources to change local conditions, but they also lack the expertise to effectively attract and manage outside resources. To them, technical assistance is a very important part of the service delivery process.

In closing, I urge you to amend the Consolidated Farm and Rural Development Act to include provisions that have been highlighted by me in my testimony as well as those detailed by my colleagues on this panel. By doing so, you will assure the smooth flow of scarce resources to the neediest communities.

Thank you.

Mr. DEWEAVER. Mr. Bruzelius, do you want to add something?

## STATEMENT OF KEN BRUZELIUS, MIDWEST ASSISTANCE PROGRAM

Mr. BRUZELIUS. Madam Chairman, I thank you for the opportunity to be here. My name is Ken Bruzelius, and it is getting late and I am getting hungry. And, besides that, I would like a glass of water, but my glass is empty. And that is the way it is with many rural communities whose neighbors have had the opportunity to get adequate water and waste disposal facilities, but they have not.

My prepared testimony is before you.[1] I would like to highlight several situations, however. We also work in Iowa and we are aware of the number of areas that are developing rural water systems.

We believe there are positive aspects to that with the support of the Farmers Home Administration. This does give adequate opportunity for the elderly and the lower income residents to have an affordable water supply as the other neighbors in the community.

To give you an example of how the Farmers Home Administration program is currently working I will describe a project in Argyle, Iowa. This southeastern Iowa community of 160 residents is an example of how it works.

This unincorporated community has failing septic systems, shallow wells with signs of contamination. The southeast Iowa community action agency in Burlington, Iowa, armed with training and technical assistance from the midwest assistance program, helped this community through the development process.

Needs assessments were done, public hearings held, community fund raising events were scheduled and preliminary studies were completed. The community has incorporated and established as their first priority the solving of their water problem.

In March, approximately 1 year after the midwest assistance program's first involvement with Argyle, they received a letter of conditions from the Farmers Home Administration which provides for the funding of the water system. This sounds like a phenomenal success—and to this community, it is. But, to those of us who work with the Farmers Home programs and with many rural communities needing this assistance, we are less than overjoyed.

Argyle is getting an $82,400 loan at 11.375-percent interest and a grant of $157,600. That is approximately a 70-percent grant. In effect, grant money is being used in Argyle to offset the difference between the 5-percent interest rate and the market interest rate. This effectively reduces the availability of grant assistance so desperately needed in other communities throughout the State of Iowa and across the Nation.

Argyle's minimum monthly user fee for 2,000 gallons of water will be $15. With this same monthly fee Argyle could have afforded a 5-percent interest loan of approximately twice that offered by the FmHA. And Farmers Home could have reduced the grant to less than $80,000, saving $80,000 in grant funds for other needy communities.

We believe the recommendations and the amendments that need to be made to the Farmers Home Administration program, as outlined by Mr. DeWeaver, would make those scarce resources available to other needy communities as well.

Thank you.

Senator HAWKINS. Thank you.

I have some questions, Mr. DeWeaver. You stated in your testimony you believed that the limited funds in the water and waste disposal facility program should be directed to the smallest and most rural communities. Could you elaborate on how you believe formal criteria should be established to determine the specifics?

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[1] See p. 141 for the prepared statement of Mr. Bruzelius.

Mr. DEWEAVER. Yes, I would. The problem is that under the current system and under the current regulations, Farmers Home has established priorities of a variety of types.

We have no particular argument with many of those priorities, and a number of them are congressionally determined. However, there is no way they can sort priorities in one application versus a competing set of priorities in another application. There is no way they can say, "We rank you on a scale of 1 to 100, and this is where you rank and this is where you rank compared to the other applications."

As a result, they have to resort to the kind of subterfuge my associates have attested to, to say, "Well, we are not sure we can make it this year. Maybe you had better come back and see us next year," or "Maybe your engineer had better not go ahead and prepare the full set of plans and specifications because we don't know if we can get to you."

There is no way a community can tell whether they were given a fair shake in terms of whether their needs were really higher priority needs, high under an objective, open statutorily determined priority system, because there is no such system, which is why we believe that a simple system with three basic factors in it—income level, community size, and severity of health needs—would be a fair system for everyone concerned, and make it a much easier system for Farmers Home to administer.

Senator HAWKINS. Do you think it is appropriate for the Secretary of Agriculture to retain discretionary authority for making those decisions?

Mr. DEWEAVER. We would see a great deal of flexibility on the Secretary's part, on the part of the people in Farmers Home Administration under a system. We are not by any means suggesting that they be put into a straightjacket. We are just suggesting that they have a rule book, which is an open rule book, which reflects congressional priorities and that everyone can follow. One can follow it by reading it at the community end and on the outside they can follow it and on the inside, rather than the current system where one is forced to conclude, looking at it from a community perspective, that the judgments are entirely subjective that go into the process of deciding who actually gets what money is available.

Senator HAWKINS. If your amendments regarding graduated interest rates and the establishment of project priority criteria are included in this legislation, is it possible that higher authorizations would be necessary to meet the requirements for all of the communities that would become eligible?

Mr. DEWEAVER. Quite candidly, Madam Chairman, we do feel that it would be highly desirable, particularly for those communities with very inadequate systems, as is the case in some of the situations my colleagues have described, that those communities stand a better chance of having decent water for their residents if there were more money available. However, we recognize that this is a time of fiscal restraint and that working from a community perspective, it is necessary to deal with the assistance that is available. We think, in fact, the recommendations that we are making, including a project selection system and the graduated assistance

under both the loan program and the grant program are even more appropriate with limited resources than they would be if we had the level of resources that were available 2 or 3 years ago. So we feel it would be easier, in fact, to implement the program, and that those kinds of changes are absolutely necessary, urgently necessary, because of the fact resources are very limited. So that while we might like to see higher authorization levels, we think that these changes are necessary, the lower available funds go.

Senator HAWKINS. As you know, and have heard, many people testified that the Farmers Home staff is already faced with an overload of work. If all the changes you have suggested were implemented, what effect do you think they would have on Farmers Home's ability to process loan requests?

Mr. DEWEAVER. We would like to think they would be speeded up because the rules would be simpler and they would be easier to understand from everybody's standpoint. And perhaps one or two of my associates might like to comment on the leadtimes that people face now when there is no clearcut rule book in terms of who gets assistance, or what level of assistance they get.

Mr. BRUZELIUS. The mayor of Goodridge, Minn. wrote me several weeks ago and we have been talking to them subsequently. Three years ago they made application to the Farmers Home Administration for a loan and grant to assist them with developing a water system. It was 2 years before they had a determination back from Farmers Home which said, "You are too poor for us to provide a loan, and we don't have adequate grant funds available."

They are still without their water system and they did not have any real way of knowing where they stood with Farmers Home during that time.

Senator HAWKINS. During the whole 2 years?

Mr. BRUZELIUS. That is right.

Mr. DEWEAVER. That is a persistent problem and, as several of the examples, including Mr. Johnson's example in Mississippi, point out, communities while they are waiting for Farmers Home to do something lose the opportunity to get resources from other agencies. So that simplifying the system, making it more predictable, we feel, would, in fact, speed it up and would make the system more workable with the limited Farmers Home staff.

Senator HAWKINS. How did you determine 80 percent of statewide nonmetropolitan median income as the proper level to establish special interest rate eligibility?

Mr. DEWEAVER. We did it, I guess, in two ways, Madam Chairman: First, we looked at the priority that has been established in the housing programs which are, obviously, related to the provision of very essential water and waste water service. And in the Housing Act, we have a standard, an 80-percent standard, which is set for housing programs in Farmers Home as well as programs available through HUD and through community development bloc grant programs. So it is a widely used and accepted measure in Farmers Home as well as in other agencies.

By contrast, the 85-percent level, which is proposed in the Farmers Home proposed regulations, is not a commonly used standard for any program.

We also looked at a number of specific States to try and establish what the impact would be of this kind of change. It seemed that communities that lay people would determine would be needy communities by most people's standards, would fall within that limitation, whereas there are severe problems now with Farmers Home use of the poverty level as the criterion for 5-percent loan money.

So, we both looked at the States and looked at the factor as ample precedent in other legislation.

Senator HAWKINS. What is your reaction to the report by the rural development advisory council?

Mr. DEWEAVER. Which recommendation is that, Madam Chairman?

Senator HAWKINS. The concept of using pension funds.

Mr. DEWEAVER. We would feel that, in fact, sources other than Farmers Home Administration should be more readily available. As the community cases that my associates described indicate, we are dealing in very small and very poor communities. And, unfortunately, there does not seem to be any alternative to the organized system that is in place now and has been for some years in Farmers Home in reaching that range of community. It is, in a way, comparable to some of the testimony earlier this morning with respect to the limited resource farmer. We have a level of need which is very difficult to meet without public assistance type mechanisms to meet it. So we would feel that improvements are needed in the current Farmers Home system and that while it is worthwhile to explore other alternatives, in the meantime we must reach communities that do not have water to drink now.

Senator HAWKINS. If pension funds were used—were approved for loan credit, would you perceive that process working in rural areas?

Mr. DEWEAVER. We would perceive that it would take sometime to establish an alternative program. There are also questions about affordability, which is a key issue, obviously, to all of our organizations, that, unless the terms were such they could really meet the need, having the money simply available would not help.

The terms under which assistance is available have to be such that a community can afford it. Otherwise, we have the example of Wheelwright, where the mayor had to write back to Farmers Home and say we are going to have to continue to use a dilapidated system because we cannot afford the particular help.

Senator HAWKINS. This probably would come in.

Mr. DEWEAVER. That would be a key factor, particularly since in a number of States, rural water services are provided by mutual water companies and other nonpublic entities. But the Farmers Home system can reach those communities. Other alternatives, generally speaking, cannot because those associations by definition lack taxing power.

Senator HAWKINS. Thank you so much for your participation here today. You have contributed greatly to our record and we appreciate your concern.

Mr. DEWEAVER. Thank you.

Senator HAWKINS. I now call Burton Milnor and William Houston.

**STATEMENT OF BURTON MILNOR, MORGAN, KEEGAN & CO., INC., GOVERNMENT LOAN COMMITTEE, PUBLIC SECURITIES ASSOCIATION**

Mr. MILNOR. Madam Chairman, my name is Burton Milnor. I am an assistant vice president with responsibility for Government guaranteed finance for Morgan, Keegan & Co., Inc., of Memphis, Tenn., a regional New York Stock Exchange member firm.

I am here today in my capacity as secretary of the Government Guaranteed Loan Committee of the Public Securities Association. The Public Securities Association represents most of the broker/dealers and dealer banks across the country who market U.S. Treasury and Federal agency securities, and securities issued by State and local government.

I am accompanied by Thomas Cator of Neece, Cator & Associates, our Washington counsel.

The committee on which I serve represents substantially all the firms in the Nation involved in providing a market for U.S. Government guaranteed loans to business enterprises. Most of the country's major, well-known securities firms are involved in this activity and are represented on our committee. Because of the national scope of our members' activities, we are in a position to observe the broad contributions made by the guarantee programs we utilize to the borrowers, the lenders, and their communities.

I would like to address my comments principally to the overall role of the Farmers Home Administration business and industrial loan guarantee program in the capital markets.

Ongoing advancement in farm mechanization and weak markets for agricultural products continue to take their toll in farm labor. Rural communities have found that their populations are expanding and that they are being hard hit by unemployment. For example, Stewart County, which is near my home, is a rural area located in Tennessee, and has experienced an increase in unemployment from 36.4 percent in November 1981 to 40.9 percent in February 1982, a period of 3 months.

The inability of the small- and medium-sized employers to obtain long-term capital, whether in the form of credit or in the form of investment, precludes startup of new industry or expansion of existing industry and resultant new jobs.

The B. & I. program was originally enacted in 1974 because small- and medium-sized employers located in rural areas had difficulty raising long-term investment capital. Without the ability to attract money from the private sector, these companies' other sources of funds are generally limited to the commercial banks in their areas. But growing companies' capital needs are not, however, easily met by a rural commercial bank.

There are three primary reasons for this: First, commercial banks in rural communities are usually small independent institutions. It follows that such a bank's net worth is usually small and since the legal lending limit—that amount one bank may lend to one borrower—is a function of that net worth, a single rural bank often cannot make a loan large enough to benefit the borrower.

Second, commercial banks are traditionally short-term lenders. While the maximum maturity policy varies from bank to bank,

generally, requests for loans with maturities beyond 7 years are denied or referred to other types of lenders.

And, third, in the rapidly growing parts of the country, the demand for credit typically exceeds the available deposits. Since a bank's total loan portfolio must be a fraction of its deposits, many rural banks find that they are too illiquid to service many commercial loans which otherwise meet their criteria.

The Farmers Home Administration guarantee specifically addresses these three problems and very often enables banks to circumvent them. To begin with, regulatory authorities have ruled that only the nonguaranteed portion of a loan is counted against the bank's legal lending limit. Thus, in theory, the bank may make a loan to a single borrower as much as 10 times its legal lending limit.

Further, the ability of a bank to sell the guaranteed portion of a loan to the private sector creates liquidity for the lender and given the further ability to retain a reasonable servicing fee on that portion sold, many banks are willing to compromise their maturity requirements. As a result, the B. & I. program fills a need which will not otherwise be met by the current banking system.

We believe that the administrative shortcomings in the B. & I. programs have been properly analyzed and that sound correctional procedures have been implemented. Recent criticism of that program has pointed to an increasing default ratio. This is only commensurate with the overall state of the economy as evidenced by a substantial increase of defaults experienced by commercial banks in their portfolios of conventional loans.

For example, according to the Federal Reserve Board's latest statistics, net loan chargeoffs or losses at the Nation's 14,000 insured commercial banks have increased from nearly $2.5 billion in 1978 to over $3.7 billion in 1981. That is more than a 50-percent increase.

Neither our industry nor we expect the lenders and borrowers who receive B. & I. guarantees are looking for Government subsidies. In our opinion, the B. & I. program has functioned in a highly successful manner in the past and acting upon the constructive criticism received over the past few years is making great strides toward self-sufficiency. Our committee believes a self-sufficient B. & I. program, enabling loans to be made in capital short regions of the country in free market transactions and without interest rate subsidies, will answer any legitimate concerns regarding the B. & I. program.

Thank you, Madam Chairman.

That is the conclusion of my prepared text. I would like to make a few extemporaneous remarks to the committee.

I have often been asked how does B. & I. help channel money to the rural areas.

The capital poor areas in the country have been made aware both by the Farmers Home Administration and by the broker/dealer community and by their associations of the existence of a secondary market for the guaranteed portion of their loans. They, therefore, can make a loan and sell that guaranteed portion. The broker who buys that guaranteed portion then, in turn, sells it to a

capital rich area of the country. In this way money goes from capital rich to capital poor areas. It is a very successful program.

That brings up the question, probably, How does the brokerage system work? To cite a very quick and easy example, if a loan is made for $1 million and has a 90-percent Farmers Home Administration guarantee, there is a guaranteed portion, therefore, of $900,000. I will buy that $900,000 portion from the bank for $900,000, with an interest rate that is acceptable to the investment community. I then turn around and sell that $900,000 portion for $904,500. I make my profit by putting the two in touch with each other.

You mentioned in your statement targeting. We are certainly amenable to that. We feel that a percentage of the moneys allocated for the B. & I. program could well be targeted to areas of low employment.

Equity requirements, I have a problem with. As a former secured lending officer with a commercial bank, I am aware that many companies in a growth mode do not have adequate equity. A large metropolitan commercial bank has means of dealing with that. Generally speaking, they do accounts receivable and inventory financing. It creates long-term credit, even though they call it a line of credit, and it works. But a rural bank is not large enough to do that labor intensive type of lending.

Equity requirements of greater than 10 percent would take out of the borrowing market many industries which indicate the ability to continue to grow healthily.

Guarantees of less than 90 percent, I also advocate to the extent that the Farmers Home Administration B. & I. people be encouraged to work with the lender to determine what guarantee percentage is needed. If you mandate a lower than 90 percent guaranteed percentage, that, too, will take many, many worthwhile borrowers out of the program.

We support freezing the authorization level of the program at last year's level of $1 billion.

I will be happy to respond to any questions you may have.

Senator HAWKINS. Thank you. That takes care of most of my questions.

Last year, the staff of the House investigative committee criticized lender servicing on B. & I. loans and recommended that when Farmers Home is requested to honor a guarantee that an audit be performed to determine the cause. If negligence by a private lender was found to be present, the staff recommended that Farmers Home should deny the guarantee.

How would you view a provision such as this be included in this reauthorization?

Mr. MILNOR. Madam Chairman, that would, in my opinion, do away with the secondary market. The investor who may be in Miami, Fla., who buys the guaranteed portion of a loan that was made in the State of Oregon has no way of protecting himself against negligence or fraud by the bank. If Farmers Home Administration denies that guarantee, then the investor would be out his money, while being totally innocent.

Senator HAWKINS. Last year the House Appropriations Subcommittee on Survey and Investigations concluded that the minimum

10 percent equity requirement on B. & I. loans was too low. Do you agree with that?

Mr. MILNOR. As I stated earlier, in my extemporaneous remarks, 10 percent is not too low across the board. Ten percent is too low, or 10 percent equity is too low in some cases. I think, again, that I would encourage the Farmers Home Administration B. & I. people to review this on a case-by-case basis.

Senator HAWKINS. Would an increase in equity requirements lower the risk of default?

Mr. MILNOR. Yes.

Senator HAWKINS. Would you agree that in light of the historically poor record of loan repayment that something must be done to protect the taxpayer from loan defaults?

Mr. MILNOR. No, madam, I would take issue with the statement "historically poor record." I think the default ratio on Farmers Home Administration loans is certainly going to be higher than that of a conventional loan portfolio of commercial banks. But we are not talking about conventional borrowers to begin with. We are talking about people in poorly capitalized areas and in the rural communities that are having some difficulty.

I do not believe that the ratio of default has gone up disproportionately with the ratio of default for conventional loans.

Senator HAWKINS. Do you have figures to support that statement?

Mr. MILNOR. Yes, madam, these were given to me over the telephone. I beg your pardon. I am sorry. No, madam, I do not. I will attempt to get figures for that and respond in writing.

Senator HAWKINS. In 1981, I have figures to show that $22 million was paid in loss settlements incurred in the B. & I. program in 1981. In 1982, the loss is expected to be $30 million.

Mr. MILNOR. Yes, madam.

Senator HAWKINS. And in 1984, losses are projected to be $40 million.

In your statement, you indicated that programs had been tightened up over the last 1½ years. What improvements can you cite that will begin to reduce these losses suffered by the program?

Mr. MILNOR. At the present time, all applications for B. & I. guarantees must be approved in Washington, D.C. This is after the State B. & I. director has reviewed them and forwarded them to Washington with his recommendations.

The credit criteria has been approved.

Second, I would like to point out that when this program was enacted in 1974, we took State people and, in some cases, county people who were familiar with farm credit but were not familiar with commercial credit and asked them to make commercial credit judgments. Over this period of the last 7 or 8 years, they have learned the hard way, and I think in most of the situations that I am aware of they have learned well.

Senator HAWKINS. In your opinion, should the B. & I. loan guarantees be targeted to rural areas where the population is declining, or to areas where the population has increased?

Mr. MILNOR. I would think that targeting based upon an increasing or decreasing population might create some problems, but I am not prepared to address that.

Senator HAWKINS. You prefer a case-by-case basis?

Mr. MILNOR. Yes, madam, I certainly do.

Senator HAWKINS. Assuming that only limited source of funding is provided by Congress for this program, should special emphasis be placed on providing loan guarantees to small businesses or to larger businesses?

Mr. MILNOR. We feel that the loans in the $500,000 to $1 million-plus neighborhood are probably more appropriately handled by a B. & I. program than the very large loans of $10, $15, or $20 million, particularly in view of the limited availability of funds.

Senator HAWKINS. Thank you so much.

Earlier the American Bankers Association testified. Were you here?

Mr. MILNOR. Yes, madam.

Senator HAWKINS. They testified that there is sufficient credit available from rural banks to fund credit for the projects that are posed for continuation. How do you explain the wide difference of opinion between yourself and the ABA?

Mr. MILNOR. I think that the ABA is making a statement which I would agree with. At the present time there is more than adequate money available for credit demands. However, the administration, as do I, believe that we are going to see an economic turnaround before the end of this year, probably during the third quarter.

Given that we have an economic turnaround, there is a pent-up demand for credit that will not be met under normal circumstances.

Senator HAWKINS. It is encouraging to hear that. Thank you. I feel the same way. Spread that word wherever you go. I appreciate it very much.

Mr. MILNOR. Thank you, Madam Chairman.

Senator HAWKINS. Mr. Houston, you represent the National Cotton Council. You did not appear with the other farmers, I understand, because the planes do not fly when you are ready; is that right?

## STATEMENT OF WILLIAM H. HOUSTON III, REPRESENTING THE NATIONAL COTTON COUNCIL OF AMERICA

Mr. HOUSTON. No, Madam, I was just scheduled to appear at this time.

Madam Chairman, we appreciate the opportunity to appear before you here this morning.

My name is William H. Houston III. I am a cotton farmer from Tunica, Miss. I am also a member of the Industry Practices and Policies Committee of the National Cotton Council, in whose behalf I appear here today.

Also with me is Mr. Charles Bragg, a representative of the Producers Steering Committee of the National Cotton Council.

The National Cotton Council is the central organization of the U.S. cotton industry, representing all sectors of the industry from producer to textile manufacturer, in the 18 cotton producing States from the Carolinas to California. Its headquarters are in Memphis, Tenn.

My purpose here today is to strongly urge this subcommittee's support for the reauthorization of Farmers Home Administration. The financial condition of the American farmer is strained almost to the breaking point, making it imperative that FmHA lending authority be continued, and hopefully, expanded.

Cotton farmers in most parts of the belt have suffered two disastrous seasons in a row, and some three.

In 1980, USDA's summary of crop production mapped drought severity by areas, indicating "moderate," "severe," and "extreme." I would like to submit that map for the record.

Senator HAWKINS. Submit it.

[The map referred to follows:]

Mr. HOUSTON. All of the Cotton Belt that depends on rainfall was in either the "extreme" or the "severe" category.

"Extreme" drought covered all cotton producing areas in Texas, Oklahoma, Missouri, and Tennessee, plus most of the producing areas of Arkansas, Louisiana, and Georgia. As a result, cotton yields in the Southwest region were 34 percent below the previous 5-year average, and those in the delta and Southwest were 18 percent and 16 percent below, respectively. These were yields per harvested acre. Many fields simply were not harvested at all. Abandonment in the Southwest hit a record 13.4 percent.

These averages are striking enough. But, when you realize that half the producers were below the average, you begin to see what their plight was in 1980.

The weather reversed itself in 1981, and near-record yields were produced. Unfortunately, this big crop—the largest in 28 years—coincided with a market that was extremely depressed because of a worldwide recession and record cotton textile imports. Prices fell some 35 percent from the previous year, and most producers lost money in 1981 despite good yields. A few were hit by drought and suffered both low prices and low production.

Most cotton farmers then, through circumstances beyond their control, find themselves in extremely difficult financial situations. Many of them have little equity left to secure production loans for

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a 1982 crop. On top of that, high interest rates add to their already heavy cost burdens.

In the past, farmers who owned their land were able to offset some of those problems through additional equity generated by rapidly increasing land prices. But, with high interest rates and low commodity prices holding down land values this year, this added source of borrowing power is not available to them. Even more significant, however, is the fact that some 60 percent of the cotton crop is grown on rented land, which, of course, affords no loan security at all.

There are those, of course, who have equity remaining in land and/or equipment. For them, the problem is one of cash flow. Those producers must have credit to bridge the time across uncontrollable natural or economic disasters.

This rather desperate credit situation for many growers could result in a lot of political pressure for a "quick-fix" that might help temporarily but which, in the long run, could be very damaging to farm income. This is another reason for hoping you will do everything possible to ease the credit problem for farmers.

We are gratified by the changes in Farmers Home Administration policies that Secretary Block announced in late January. And we were especially pleased with his statement that the action was intended "to keep farmers in business during these cloudy times."

In his press conference, the Secretary said credit problems are worst in the Texas High Plains, the Mississippi Delta, and southern Georgia—all important cotton-growing areas.

One obvious inequity in the Farmers Home Administration program must be corrected, but that change will require legislation. In 1978, a statutory ceiling of $100,000 was mandated for Farmers Home Administration operating loans. USDA calculates that the average cost of cotton production increased 55 percent between 1978 and 1981. Their estimates show that the average cost to produce an acre of cotton in 1981 was $405, not including land cost. Should a producer need to borrow that amount, the $100,000 would finance only 246 acres of cotton. According to the latest agricultural census, 29 percent of the U.S. cotton producers have acreages exceeding that figure. Even more important, those 29 percent farm over 75 percent of the cotton acreage, and produce over 80 percent of the crop.

Farmers Home Administration policy is now clearly discriminating against the larger and medium size farms and more efficient growers who produce the greater part of the U.S. cotton crop. The limit must be increased to reflect inflationary cost increases since 1978 if these producers are to be able to use Farmers Home Administration lending services.

We believe that Government credit for the purpose of keeping in business farmers who have a chance for future contributions is an investment in our Nation's future, not an expense. We hope that this credit can be made available at the lowest possible rates consistent with budgetary constraints.

One way of making more credit available to financially troubled farmers without additional Government outlays would be to subordinate existing Farmers Home Administration loans to new loans from the private sector. In meetings with Assistant Secretary

Frank Naylor and Farmers Home Administration Director Charles Schuman here on January 27, we were assured that they intend to use that whenever and wherever possible. That will, of course, require the full cooperation of the Farm Credit Administration and the private banking system.

Agriculture is the backbone of our Nation's economy. It provides our country's food and fiber need at a cost which is the smallest proportion of per capita income anywhere in the world. It employs millions of persons directly on the farm, and tens of millions more in the production and distribution of the machinery, chemicals, and other supplies necessary for farm production. The income farmers spend in the small towns and cities is multiplied many times over as it moves through the channels of trade. In addition, agricultural exports are expected to approach $50 billion in foreign exchange to help pay for oil and other essential imports. In doing so, they have a strong anti-inflation influence.

Agriculture is unquestionably an essential industry that must be kept strong if our Nation is to remain strong.

Thank you very much, Madam Chairman.

Senator HAWKINS. Thank you. I have an appointment shortly and I would like to be brief, but wind this up with questions to you.

I would like to ask the same question I have asked the other representatives of farmers who have testified earlier today. How do you view the current proposal to grant a moratorium on Farmers Home loans?

Mr. HOUSTON. Senator, we have no position on a moratorium. However, I feel a moratorium would limit USDA's flexibility to a great degree. I feel like the question of deferring repayments should be handled on a case-by-case basis.

I would also like to say though that I think foreclosures would be the worst thing in the world for the farm economy and for the Farmers Home Administration. A moratorium would have a snowballing effect on decreasing land values and decreasing equity.

Senator HAWKINS. You mentioned in your testimony that the credit problem could result in a lot of political pressure for a "quick-fix" that might help temporarily but which could be very damaging to farm income in the long run.

Could you further explain that to me?

Mr. HOUSTON. Speaking there, something like an increase in price supports, loans to a level that would make us noncompetitive in the domestic and foreign market.

Senator HAWKINS. To your knowledge, is the Farmers Home Administration subordinating existing Farmers Home loans to loans in the private sector?

Mr. HOUSTON. To my knowledge, they are.

Senator HAWKINS. Thank you. We appreciate your input and experience in the very serious problems and programs before us, and giving us a very valuable record for the whole committee to base their decisions on.

Before we conclude today's hearing, I would like to place letters from the Independent Bankers Association of America and the Na-

tional Rural Electric Cooperative Association [1] in the hearing record.

We will adjourn the hearing at this time.

[Whereupon, at 12:35 p.m., the subcommittee adjourned, subject to call of the Chair.]

[1] See p. 144-146 for the above-referred-to letters.

## STATEMENT OF HON. DAVID PRYOR, A U.S. SENATOR FROM ARKANSAS

Mr. Chairman: I appreciate your calling these hearings today and including such a wide spectrum of witnesses who can knowledgeably testify concerning the many aspects of the Farmers Home Administration's Program.

The actions we take this year with respect to reauthorization of this program will perhaps be more crucial to American farmers and thus to our entire economy than in any previous time in our economy.

We face a crisis in agriculture. We've seen more farmers declaring bankruptcy or being foreclosed than in any year since the Great Depression. Many of these people have done nothing but farm. They know nothing else. What are we going to do to help them?

I'm not a great forecaster and I'd like to think that this has been the worst year farmers will see. However, unless farm prices pick up drastically and our economy takes an upswing. I'm afraid 1982 will be just as bad or worse and the Farmers Home Administration programs must be in place and adequately funded in order to handle this situation.

Many of us realize that over the past years the Farmers Home Administration has expanded and like many government programs has outgrown its original purposes of being a lender of last resort. For several years, anytime a constituent, municipality or business had a problem in rural areas, he expected Farmers Home Administration to come through with a low interest loan or a grant to solve it.

At a time when we are trying to cut back all programs, a severe look at the original focus of Farmers Home may be in order.



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But, what we have to keep in mind is that original purpose--a lender of last resort. And, that is exactly what they are being called upon to do at this point...and I'm afraid they just haven't been able to live up to that task.

Although the Secretary of Agriculture has allowed certain adjustments in programs to be made to meet the needs, I don't think the Administration has gone far enough. Many of us around this table have urged the full $600 million funding of the Economic Emergency Loan Program for if our farmers aren't in a state of emergency now, I don't want to see one occur. It is true the Secretary has drawn up guidelines for implementing the Emergency Loan Program, but from what we've seen they're too stringent to do any good.

We've asked that the Secretary use his discretionary powers to declare a moratorium on certain foreclosures, defer repayments and allow reamortizing and rescheduling of loan repayments at not more than the existing rates.

All of us around this table are terribly concerned about our budget constraints and the shape of our economy. We don't want to spend one penny more than necessary. However, I think those of us here realize that Agriculture is unique. It is that one basic enterprise that reaches into every sector of this country's economy. It affects every citizen. Its health or sickness is a mirror of our country's financial state.

And while its condition is now one of pain, I firmly believe that once agriculture regains its balance and gets on its feet, it will lead this country back to more prosperous times. It is up to us, through programs such as this, to help it regain its balance.

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STATEMENT OF CARL T. FREDERICKSON, SENIOR DEPUTY GOVERNOR, FARM CREDIT ADMINISTRATION

Madam Chairman, my name is C.T. Fredrickson. I am Senior Deputy Governor of the Farm Credit Administration, the independent Federal Agency that regulates and supervises the cooperatively owned Farm Credit System. Before discussing current agricultural credit conditions, I would first like to provide some background information on the Farm Credit System and the Farm Credit Administration.

Farm Credit System

The cooperative Farm Credit System consists of federally chartered instrumentalities that operate under authorities contained in the Farm Credit Act of 1971 (P.L. 92-181) and other statutes, most notably the Farm Credit Act Amendments of 1980 (P.L. 96-592). The Farm Credit System provides credit and closely related services to farmers, ranchers, producers and harvesters of aquatic products, agricultural and aquatic cooperatives, rural homeowners, and certain businesses that provide farmers and ranchers with services essential to their on-farm operating needs.

While the U.S. Government provided the initial funding for the various institutions of the Farm Credit System, this "seed capital" has since been repaid. The Farm Credit System is now entirely borrower owned and controlled. Even the costs of the Farm Credit Administration (FCA), the independent Federal Agency that examines and supervises this System, is assessed upon the banks it supervises; therefore, it is the System's borrower's and

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not the taxpayers who pay the expenses of the Farm Credit Administration.

The Farm Credit System obtains its loan funds primarily through the sale of securities in the national and international money markets. These securities are not guaranteed by the U.S. Government. They are sold through the System's Fiscal Agent in New York City.

The three agricultural credit systems that comprise the Farm Credit System are described below.

The 12 Federal land banks (FLBs) make loans ranging from 5 to 40 years through local Federal land bank associations (FLBAs). These loans must be secured by first liens on farm or rural real estate or their equivalency. Loans may be made for a variety of purposes, including the purchase of farms, farmland, and farm improvements; rural homes and real estate needed for farm-related businesses; the purchase of equipment, machinery, and livestock; refinancing existing mortgages and paying other debts; and financing other needs of the borrower.

The Federal intermediate credit banks (FICBs) provide loan funds to local production credit associations (PCAs) and discount the notes of eligible borrowers given to other financing institutions. The FICBs may also participate with production credit associations, commercial banks, and one another in making loans.

PCAs make loans with terms up to 10 years to farmers, ranchers, rural homeowners, and certain farm-related businesses. They also

make loans with terms up to 15 years to producers and harvesters of aquatic products. Loans are made for a variety of purposes related to the production of agricultural products, the production and harvesting of aquatic products, the purchase, repair, or maintenance of rural homes, and other requirements of the borrower.

The banks for cooperatives (BCs) serve agricultural, aquatic and rural electric cooperatives whose headquarters are within their respective districts. The BCs provide cooperatives with a complete credit service designed to fulfill their specialized needs. The banks for cooperatives make term loans for purposes such as constructing, remodeling, or expanding facilities, or for purchasing land, buildings, or equipment. Seasonal loans are made to finance current or seasonal assets.

The Central Bank for Cooperatives participates with the district banks in loans that exceed their individual lending limits. The BCs may also participate with one another and with other financing institutions in making loans.

The Federal Farm Credit Board is the top policymaking body for the Farm Credit Administration and the cooperative Farm Credit System. Members of the Federal Farm Credit Board, as those of all other boards in the System, serve on a part-time basis. Twelve members of the Board, one from each Farm Credit district, are appointed by the President of the United States with the advice and consent of the U.S. Senate. They serve 6-year terms and are not eligible for reappointment. A 13th member of the Board is appointed by and serves at the pleasure of the Secretary of Agriculture.

The Governor is the Farm Credit Administration's chief executive officer. He is appointed by and serves at the pleasure of the Federal Farm Credit Board. He is ultimately responsible for carrying out the policies of the Board by ensuring that the Farm Credit Administration supervises, examines, and regulates the Farm Credit System in the public interest. At the same time, each institution of the System is a user-owned and controlled cooperative association. A great deal of responsibility for directing and managing Farm Credit institutions is vested in member-elected boards of directors and their selected management. FCA supervision is designed to oversee the actions of the district boards to ensure sound management of the banks and associations. Operating decisions are decentralized within the System to the user level, as long as System objectives are respected and sound business is conducted.

## Farm Financial Conditions

Now, let us take a look at the agricultural economy. It is not news that there are economic problems in agriculture today. They are extremely widespread, covering virtually the entire spectrum of production agriculture, and they are serious. Net farm income last year was $23 billion -- about $4 billion of that is associated with an inventory buildup. The current projection for farm income for 1982 hovers between $13 and $18 billion. These numbers compare with an all time peak of $33 billion in 1973. In constant dollar terms, net farm income in 1982 could be about one-fifth what it was in 1973.

At first blush, agricultures' aggregate balance sheet appears quite reassuring. Total agricultural debt at the end of 1982 will exceed $200 billion, an all time high. But, total assets are in excess of a trillion dollars. The debt-asset percentage is less than 17, which is very low in comparison with industry. That reassuring first impression is terribly misleading, however. The ratio of total debt to farm income this year will likely be over 13:1 as compared with less than 3:1 in 1973. One indication of the weight of that debt burden is the fact that interest expenses in 1981 accounted for 13 percent of total production expenses.

In order to fully appreciate the extent to which the aggregate balance sheet is misleading, one must understand the amount of leverage employed by the commercial sector of agriculture, i.e., by farms with annual sales in excess of $40,000. If it were possible to examine the balance sheets of these 500,000 - 600,000 farms, we estimate the debt asset percentage would be almost double that of agriculture in total. Many individual commercial farms could have debt-asset ratios that are quadruple the national average. While it is true that these farms receive a very large proportion of total agricultural income, the heavy use of debt makes many of them particularly vulnerable to income fluctuations.

The income and financial outlook for farmers in 1982 is a matter of serious concern. The prospect of a sustained 3-year decline in net cash income from farming raises obvious questions about the ability of some farmers to maintain productive operations. Since 1979, overall prices received by farmers have increased only 4.5 percent, while prices paid have increased about 22 percent. In

each of the past 2 years, the nominal gain in the price of agricultural assets has been less than the general rate of inflation, resulting in a decline in the real wealth position of agriculture. In 1981 alone, the purchasing power of farm assets decreased almost $12 billion, according to preliminary estimates. While this drop would be only about 1 percent, we suspect it will turn out much steeper when yearend land value data become available. Successive declines in real asset values is in marked contrast to the mid-1970s, when net operating returns were modest, but capital appreciation was large in both nominal and real terms.

The main sources of optimism for 1982 are the potential for a reduced world crop and the prospect that some significant proportion of the July 1 individual tax reductions will be reflected in consumer demands for meat and other food products. The extent of producer participation in the voluntary feed grain and cotton acreage set-aside programs, announced on January 29, will also have a significant impact on markets. Grain prices are a mixed blessing. Adequate supplies translate to low feed costs for livestock producers, thus putting a brake on the upward trend in production costs at least for that sector. Adequate supplies and slack demand, however, mean low gross income for grain producers, who will experience continued increases in their production costs. We can thus conclude that at best the overall farm financial situation is unlikely to show any improvement through mid-year.

Credit Status

The Farm Credit System is serving more borrowers and providing more loan funds than at any other time in its history. The number of FLB loans outstanding for the year ending February 28 increased by 8.4 percent to 650,962, with an aggregate amount of $47.3 billion. The number of PCA loans outstanding over the same period increased fractionally to 377,294, with February 28 outstandings of $21.1 billion. An additional $858 million was outstanding from FICBs to other financial institutions. Bank for cooperatives borrowers decreased by 68 during the 12 months to 3,509, and they held $9.8 billion in outstanding loans at the end of February. Further, overall performance of the loan portfolio has been generally acceptable through the 12-month period.

While aggregate totals are at an all-time high, growth in System loans outstanding has been slowing throughout the past year. Total loan volume outstanding in the Farm Credit System actually dropped in November, compared to a month earlier, and did not fully recover to the October peak until January. The November decline was the first month-to-month decline since November 1975 and amounted to 2.7 percent on an annual basis, compared to a 1.2-percent decline in that earlier period. As of the end of February, total System outstandings reached $79 billion, up 11.5 percent from a year ago.

The uncertain economic climate of the agricultural sector is reflected in different ways in the land bank, production credit and bank for cooperative systems. I will discuss each in turn.

FLBs

The dollar volume of loans closed by FLBs turned downward in the first 2 months of 1982. For January and February 1982, the monthly average volume of FLB closings was about 81 percent of the volume closed in the first 2 months of both 1980 and 1981. Repayments surged in December 1981 and January 1982, most probably in response to a large injection of cash into the farm sector by the Commodity Credit Corporation. The net result was continued moderation in the rate of growth of FLB loans outstanding. FLB outstandings grew at an annual rate of 11-12 percent, down from an average of 16.5 percent in the fourth quarter of 1981 and from 21.1 percent in the first 2 months of 1981.

As is to be expected in protracted periods of low farm income, there have been notable shifts in the purpose of FLB loans. Prior to 1980, roughly 10-12 percent of the dollar volume of FLB loans made was used to refinance short-term, nonreal estate loans. In 1980, 15 percent of the total volume of FLB farm loans was used for this purpose. After declining to an average of 14 percent in 1981, the percent of FLB loans made to refinance short-term debt jumped to 18 in February of this year. A similar share of FLB loans made during mid-1980 went to refinance short-term, nonreal estate debt. Despite this shift, the share of FLB loans made that is used to finance current farm operations, including purchase of machinery and equipment, remains constant at around 3 percent. Contrary to some expectations, the share of FLB loans made to refinance other FLB loans has remained rather stable at about 20 percent.

PCA/FICB

After rising briskly for the first 7 months of 1981, the dollar volume of PCA loans outstanding has declined in every month since last August. The monthly volume of PCA loans made has been below year-earlier levels since October, while collections have generally stayed above year-earlier levels. The net result was that PCA loans outstanding at the end of February stood only 2.4 percent above year-earlier levels. This reflects not only the uncertain prospect for positive net returns from agricultural production this year, but also the substitution of CCC and FmHA credit for PCA loans.

During February, 45.4 percent of the dollar volume of PCA loans made were classified as renewals. Although February is typically a heavy period of loan renewal, this is the largest share of PCA loans made that have been renewals since records of this type began being kept in January 1969. The February 1982 figure exceeds the previous maximum of 45.3 percent recorded in February 1978 by only a slight margin.

BCs

After declining in most of the first 6 months of 1981, total BC loans outstanding have generally increased on a monthly basis since last July. Since then, BC loans outstanding have grown at an annual rate of 16.7 percent. Competition from other lenders, notably CCC, has caused relatively wide month-to-month variations in the volume of BC loans made. For the first 2 months of 1982, the average volume of BC loans made ran about 90 percent of the comparable period a year ago.

Overall BC repayment rates were 101.1 percent of the 1978-80 average during 1981. For the first 2 months of 1982, the average BC repayment rate stood at 105 percent of the 1978-80 average. Repayment rates were particularly strong in the Columbia, St. Louis, and Sacramento Districts during January and February. They were off considerably, however, in the Springfield and New Orleans banks.

Farm Credit System and FCA Actions

The continuing purpose of the Farm Credit System is to provide sound, adequate, and constructive credit, in good times and bad. The ultimate test for continuing to extend credit is whether there is a reasonable prospect for financial recovery. Forbearance will continue to be our philosophy and program during 1982. We are now in a period, however, in which financial limits for some borrowers are likely to be tested. Our policy is to work with distressed borrowers so long as a reasonable prospect for recovery can be identified. Nevertheless, our forbearance philosophy also provides for counseling those who have little hope for financial survival. In such cases, we may encourage them to withdraw their remaining equity before it is dissipated.

The overriding constraint on the ability of the System to stick with borrowers in financial difficulty derives from the need to protect the financial health of the Farm Credit System. This protection is absolutely essential to ensure an adequate supply of future credit to the farm sector as a whole. Risks will be assumed, but they must be controlled so as to maintain the quality of System bonds sold in the securities markets. The System has

set aside large reserves, which serve as our first line of defense for periods in which the System must assume such risks. But it is neither realistic nor prudent to guarantee all borrowers continued access to credit regardless of their economic propects, and particularly during an extended series of poor years such as 1980, 1981, and 1982.

The System does not expect a great number of foreclosures during 1982. We do expect a significant increase in loan servicing activity, involving a larger number of borrowers. Servicing steps will include careful planning, based on cash flow prospects, and full use of the protection afforded by crop insurance, commodity credit loans and other Government programs. In addition, extensions, debt restructuring, and reamortizations will be used, where appropriate. Some sale of assets will be needed in some individual situations to solve extreme problems.

Both the banks and the Farm Credit Administration are making extra efforts to monitor the credit situation on a regular basis. We are implementing a special reporting mechanism for banks that will provide needed data on a quarterly basis. We will be sharing that with credit officials in the Administration and the Congress as the situation warrants.

Thank you Mr. Chairman.

STATEMENT OF EDWARD ANDERSEN, MASTER, NATIONAL GRANGE

Madam Chairman and members of the Committee:

I am Edward Andersen, Master of the National Grange. Our organization is grateful to you and your subcommittee for calling this hearing to discuss the credit situation facing American Agriculture and the proposed legislation S. 2314, which will authorize funding levels for specific Farmers Home Administration loan programs. I would first like to present our views on the current problems involving credit and low farm income in America. Our specific comments to S. 2314 are summarized at the end of my statement to the Committee.

Madam Chairman, the Grange is seriously concerned about the low level of net farm income. Agriculture is entering its third year of depressed prices, and many farmers and ranchers are facing bankruptcy as a result. Without a doubt, the single largest factor contributing to the crisis is the high cost of borrowing money. Agriculture is dependent on the credit market to finance production costs. Never before has farm debt been so high and so costly, and many producers are in the position of having to make capital investments that they delayed two and three years ago believing that credit would become cheaper and commodity prices would improve. The replacement of worn machinery or the production expansion planned for years before cannot be postponed much longer in the hopes that either the interest rates will drop or farm prices will rise to at least break-even levels.

There is no shortage of lending capital in the credit institutions which serve agriculture. What must be discussed today is the issue of farm income. Today's commodity prices are too low to allow farmers to borrow to their needs. Forecasts for 1982 farm income are so dismal that lending institutions must be cautious and loan only to those producers with assets not yet encumbered. There are very few of those producers left after two disasterous years of low prices and prospects for yet another in 1982.

Secretary Block is aware of the problems facing ranchers and farmers, and he has taken modest steps toward tempering the Farmers Home Administration foreclosure policy. His efforts in coordinating the Farm Credit System with private lenders is commendable, however, the objectives of this program are long term; agriculture is in need of immediate assistance. The Administration's emphasis is on graduating FmHA lenders to private or FCA sources. I submit that this

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policy, although it has merit and has Grange support, is inappropriate unless farm income improves to levels that make graduation possible. Certainly, the Secretary understands this incongruity, but he chooses to justify it on the basis that we will raise farm income through aggresive exporting and token acreage reduction programs. Modest acreage reductions and increased exports at prices below the cost of production will not remedy the ills of the agricultural economy.

Madam Chairman, I don't share the optimism of those who say that agriculture has a bright future. We've heard this before, and it may well be true. But there is only one future that matters to most of America's agricultural producers--the immediate future. And that future is mighty bleak. When better times finally come, it will be too late for many American family farmers. An immediate infusion of moderately-priced capital is all that will save many farmers and ranchers from bankruptcy. The Grange has urged the Secretary to immediately exercise his authority and open FmHA's Emergency Economic Loan Program at the full $600 million level. These EE loans should be made available to current FmHA borrowers who have made an honest effort to repay their loans but who could not overcome the low prices for their commodities and new FmHA borrowers who have been unable to obtain credit from their traditional sources.

Obviously, the Secretary has not taken our advise. The EE loan fund still sits unused while farmers and ranchers are being told that there is no shortage of capital to finance production. Perhaps the Grange and all the other major general farm organizations have not made this request clear enough. Farmers and ranchers are not telling us that banks and investment firms have no money to lend. They are telling us that they're out of unencumbered assets, the cash-flow posture in agriculture is too strained, and land values are decreasing in some areas. Producers are telling us that they can't qualify for loans at any price because lenders can't take the risks that are present in today's farm economy.

Certainly, a healthy economy would strengthen farm prices. High interest rates and a sluggish economy are depressing consumer demand--domestic and international--for farm products. After all, Madam Chairman, the current farm depression preceeded the general economic downturn, and improved net farm income is necessary to achieve economic recovery. Stable food and fiber products are a sign of a strong economy, but stable prices must be profitable prices. Net farm income must improve in order to assure supplies of quality products for consumers at reasonable prices. This country cannot

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allow its farmers and ranchers to pin their only hope for profits on the possibility of crop failures in Brazil, in Russia, in Australia, or in Europe.

This country stands to lose many of its most efficient farmers not because they can't compete, but because they cannot justify the risk of financial failure for such meager returns in the long run. Most of the farmers and ranchers whom I represent are not looking to get wealthy; they just want to make a reasonable profit on the investments and upon the risks they are assuming. Reasonably priced credit with a farm program designed for better prices will provide the necessary encouragement to assure a strong competitive agricultural economy. The Grange believes that the Secretary should release the EE loan funds, and in addition, he should exercise the discretionary authority he sought in the 1981 Farm Bill to raise CCC reserve and regular loan rates and take further steps to provide more incentive for farmers to participate in the Reduced Acreage Program.

The Farmers Home Administration serves a vital function in providing encouragement to producers. It must be funded adequately to meet the needs of struggling farmers and ranchers. Adequate FmHA funding does not preclude this Administration's goal of graduating lenders to other credit sources; it will, in the long run make that graduation possible. The National Grange has written Secretary Block and Under Secretary Naylor supporting this Administration's efforts to redirect the FmHA back to an agency serving production agriculture. We support the elimination of Business and Industrial lending, we support increased emphasis on operating loans, and we are encouraging the training of FmHA loan officers in agricultural lending practices. In addition, the Grange applauds steps taken by FmHA to target community facility loans to "truly rural" communities. And we are encouraged that producers are being urged to graduate to conventional sources of credit.

The Grange endorses S. 2314 with one suggestion for improvement. We urge that the bill earmark not less than 25 percent of FmHA insured farm ownership and operating loans for low income (limited resource) borrowers. We feel that it is a necessary provision although I am sure that FmHA will be lending nearly 100 percent of its funds to low-income borrowers this year. During more normal economic times, it is appropriate that FmHA set this amount of money aside to provide encouragement to beginning or distressed producers.

Under current direction, the Grange is convinced that FmHA fills

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a necessary role in agricultural production. It was designed to take risks, and to share in risks, which conventional lenders can not assume. It must continue to be a reliable lender of last resort or many family farmers who are faced with credit problems, due to depressed commodity prices, will be forced out of agriculture. We will not only be denied their contribution to the food and fiber supply, but we will lose their most valuable contribution as a member of our rural society.

Thank you for providing the Grange this opportunity to present our views on the credit problems facing agriculture and the proposed FmHA lending authority. I'll be glad to answer any questions you or members of the Subcommittee may have.

STATEMENT OF JAMES R. EATHERLY, CHAIRMAN, AGRICULTURAL BANKERS DIVISION, AMERICAN BANKERS ASSOCIATION

Madam Chairman and members of the Committee, I am James R. Eatherly, Chairman and President of First National Bank of Tonkawa, Oklahoma. I am testifying today in my capacity as the Chairman of the Agricultural Bankers Division of the American Bankers Association. Our Association consists of more than 13,000 full service banks, over 90% of the nation's banking community.

While our members range in size from the very smallest to the very largest banks, approximately 90% of them have assets of less than $100 million. Two-thirds of the nation's full-service banks are in communities of less than 25,000 people. In fact, half of these banks are in towns with fewer than 5,000 residents. According to the lastest estimates, nearly 60% of these community banks listed agriculture as the single most important source of income for their communities.

Banks are deeply interested and involved in the agriculture sector of the economy. At the end of 1981, commercial banks provided an estimated $30.40 billion in operating loans to farmers and an estimated $8.97 billion in mortgage loans secured by farmland. These figures are large in both absolute and relative terms and indicate the substantial involvement of banks in farm lending. Much of this farm debt is provided by smaller banks in rural areas.

Thank you, Madam Chairman, for this opportunity to present our Association's views on S. 2314, a bill to amend the Consolidated Farm and Rural Development Act. S. 2314 would continue FmHA's farm real estate and production loan programs at the $2.2 billion level, and would raise the production loan authorization from $1.375 to $1.51 billion a year. It proposes a ceiling of $1.54 billion on the disaster emergency authorization, and provides for loan authorizations of $300 million for water and waste disposal project loans, and $130 million for loans to finance other community facilities in rural communities that have no other source of assistance.

The bill does not request authorization to continue the business/industrial loan guarantee program; and would terminate authority for non-emergency farm loans at subsidized interest rates. The American Bankers Association supports S. 2314. We believe, however, that the issues involved in this legislation need to be considered in a somewhat broad context. Specifically, we believe that the operation of the Farmers Home Administration should be examined in relation to the whole structure of this country's financial institutions and the credit needs of the agricultural sector of the economy.

Of the major public agencies that lend directly to farmers, the Farmers Home Administration is the largest and the most important in terms of reflecting the credit policies and structural interest of the Department of Agriculture. In 1981, the Farmers Home Administration portfolio was nearly 50 times its size in 1960, with more than $14 billion in grants and loan obligations extended in 1979 alone. In approximately six years, the Farmers Home Administration's share of total farm indebtedness had risen to 14% from 4%.

Any Federal credit activity involves some degree of subsidy. In essence, a subsidy is granted when a borrower obtains funds at an interest rate lower than would have been paid for a comparable private loan. A study by the Federal Reserve Board indicates that this kind of subsidy amounted to about $24 billion in 1980.[1]

The Federal Government "crowds out" private borrowers in two significant ways. Much public attention has been focused on direct Federal borrowing for financing budget deficits. Less well known is the growth in private sector loans that are guaranteed by the government. Guaranteed loans rose from over $45 billion in 1978, to over $60 billion in 1979, to nearly $69 billion in 1980, to more than $90 billion in 1981.

According to the Department of Agriculture, between 1979 and 1982, farmers had to spend 20% more on interest charges, fertilizer, fuel, farm machinery and other components necessary to raise crops and livestock. During the same period, prices at which they sold the crops and livestock grew by less than 5%. High domestic interest rates have meant the cost of borrowing to finance farming is much too high; and, industrial purchasers, reluctant to tie up costly capital, are not stocking up on commodities they do not need immediately.

Net farm income may slide as low as $14 billion or $14.5 billion in 1982, a 3% decline from the estimated 1981 figure of $22.9 billion and a significant drop from the $16 billion to $19 billion figure used at USDA's November 1981 outlook conference.

For the first time since 1969, the value of farm exports in expected to fall. In mid-February, USDA predicted that the volume of exports would grow by about 4% in 1982 but "lower prices for most major products will likely reduce the export value to around $42.5 billion." That compares with a 1981 level of $43.8 billion. During the last quarter of 1981, exports declined 4% in value. Total farm debt rose 11% in 1981, while the value of total farm assets increased only 8%.

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[1] Special Analysis F, Special Analyses, Budget of the U.S. Gov't, Fiscal Year 1982, Table F-11.

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The continuing high and volatile levels of interest rates are, of course, at the heart of the present economic difficulties. Banks are extending their resources to carry existing borrowers sometimes beyond the limits of creditworthiness. In a recent report to Congress prepared jointly by the Small Business Administration and the Federal banking agencies, over 75% of small businesses surveyed indicated considerable satisfaction with their banks' efforts to assist them with financing. At the same time, virtually all respondents decried the level of interest rates as causing them financial difficulties. It appears that most banks have engaged in loan renegotiation, interest only payment plans, extension of loan maturities, and even significant rate reductions to assist struggling small business and farm borrowers through the current difficult period.

It must also be pointed out that, while reduced Federal deficits would provide relief from high interest rates, the cutback in Federal credit and grant programs needed to move toward a balanced budget have eliminated some of the governmental funds on which cooperative private/public lending programs have been premised. Thus, while high rates have caused many potential loan applicants to abandon borrowing plans, government-assisted loan programs are becoming less available as alternatives to private borrowing.

Most public comment on high interest rates has emphasized that the Federal Reserve Board, in maintaining a "tight money" policy aimed at reducing inflation also reduces the supply of credit available to borrowers -- thereby raising interest rates. What is rarely pointed out, however is that the Federal Government is also exerting tremendous influence on the demand side of credit markets. The use of Federal credit programs (loans and loans guaranteed) has doubled in the past 4 years (1977-81), from $71.6 billion in 1977 to an estimated $147.3 in 1981, and during the same period the nation has experienced record-high interest rates. Even though strong pressures are being exerted for the growth to continue, the President has indicated that forceful actions will be taken to restrain government loan growth during the 1982 fiscal year.

Agriculture has changed dramatically over the last few years. The average size of the production unit has become increasingly larger and these units have become more capital intensive. Farmers' capital and credit needs are growing at record paces. During the 1970's, the average annual increase in debt exceeded 10.5%. In most recent years the growth rate in debt outstanding exceeded 15% per year. Farmers are expected to continue to increase their use of debt financing in the decade ahead. General economic, fiscal, and monetary policies directly and in-

directly impact on money-market conditions and thus are important determinants of the availability and cost of borrowed funds to farmers.

Farm production expenses will more than double in the 1980's. Funds needed to finance annual farm production expenses could increase to more than $200 billion over the decade, compared with about $134 billion total farm production expenses in 1980. According to a study published by the Department of Agriculture, farm-sector debt, which increased from $12 billion in the 1950's to $158 billion in 1980, could be about $600 billion by the end of the decade.

Madam Chairman, borrowed funds to finance expanded output and rising costs have become the lifeblood of modern agriculture The Agricultural Bankers Division of the ABA conducted a survey to assess the financial conditions of farm borrowers. Results of the survey show that in comparison to that of 1980, the current and anticipated situation for funds availability at banks is good. Current demand is somewhat lower than a year ago partly because of more careful financial planning, general uncertainty of the economy, and high short-term interest rate levels.

Some of our other findings are as follows:

1. Year end 1981 financial statements show expected declines in net worth and deterioration in financial ratios.
2. The primary limiting factor on use of credit in 1982 will be the debt servicing ability of farmers.
3. Farm loan delinquencies and defaults are higher than normal, and higher than one likes, but currently do not reflect a crisis condition.
4. Most bank farm customers will survive the 1981 season, with the most stressed situations being in the cattle areas of the West and Southwest and extended drought regions of the South.

In summary, the deteriorated financial condition of farmers is primarily due to low livestock and crop prices (and in some areas by below average yield), high interest rates, and high operating costs. This has been accompanied by a general decrease in value of inventories and capital items resulting in a decline in net worth. We bankers, Madam Chairman, are very concerned about the farm economy of 1982.

The solution to the farm economy is not more loans - but improved income. Additional authorizations for the Farmers Home Administration should be primarily through the guaranteed programs allowing private lenders to make loans within reasonable time periods at market interest rates. The Farmers Home Administration

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direct loan program should be "stretched" through the use of subordinated collateral arrangements in coordination with private lenders.

The ABA supports the Administration's basic philosophy of a reduced budget for Farmers Home Administration programs. The Economic Emergency and Business and Industry lending programs of the Farmers Home Administration have been singled out for Federal funds reduction and eventual elimination.

The Economic Emergency loans are for those who suffer economic losses or a general lack of credit or unfavorable relationships between production costs and agricultural commodity prices. The emergency lending programs tend to reduce the overall threats farmers face from the weather and in the market and thus have contributed to farm consolidations and higher land prices. The magnitude of their impact may be suggested by the growth in the relative importance of emergency loans. Currently, total public emergency loans outstanding constitute almost 10% of total outstanding farm debt. The emergency lending programs are like free insurance programs. They substitute for sound insurance programs and discourage the development of other private and/or individual risk-management strategies.

Specifically, efforts to alleviate the impact of natural crop disasters have been duplicative and at times ineffective. The reduction in the funding of the Economic Emergency program does not necessarily constitute a serious coverage gap, since there are other alternative programs available. There are several privately owned crop insurance companies that are competing to satisfy the needs of American farmers. The Federal Crop Insurance Corporation, for instance, which has been expanded and modified to cover all-risk and all-county, can and will be used to accommodate farmers' crop insurance needs.

Since the Economic Emergency program is duplicative, it would be appropriate to eliminate it.

The Business and Industry loan program was first established under the Farmers Home Administration to provide government guaranteed loans for projects that would provide employment to improve, develop or finance business or industry in a rural area. There are no dollar limits on the size of the Business and Industry loans that Farmers Home Administration can or will guarantee, and there is no requirement that a borrower be unable to obtain credit form other sources.

Much of the recent expansion of the Farmers Home Adminsitration has been in non-farm programs such as housing, community facilities, and Business and Industry loans. Even though we support the goals of the Business and Industry loan program for the industrial development of rural America, it should be pointed out that this program

is not a production agricultural program.

The Business and Industry loans have been beneficial to the rural communities. However, in the spirit of a joint national struggle against our weak economic enviornment, the Association supports the comprehensive package of the Administration's spending reductions.

We believe that full-service banks are the most appropriate entities to mediate between the needs of agriculture and business and industry in rural areas. Banks are not only well established in such areas, but understand the economic needs of the areas and the most productive uses of credit resources. Thus, it seems much more sensible to have loan decisions made by local institutions instead of a Federal entity. If the Federal government wishes to lend its support to industrial development in rural areas, a Federal guarantee of loans by private institutions is certainly preferable to direct lending by a Federal entity. However, the use of such guarantees should be consistent with overall economic goals, and we would not recommend expanding their use at this time.

As a result of the proposed funding cuts by the government, the Farmers Home Administration will have to narrow its focus to those borrowers who lack access to other credit sources and not serve as a source of below-market interest rate loans and loan guarantees to a wide variety of private credit-worthy borrowers, as it has in the recent past.

Thank you, Madam Chairman, and I will try to respond to questions from you and other members of the Committee.

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[The following attachments were submitted by Paul Sacia, National Farmers Union, see p. 58 for oral reference.]

ATTACHMENT A

NATIONAL FARMERS UNION 1982 POLICY STATEMENT

OF 80TH ANNUAL CONVENTION

WASHINGTON, D.C., FEB. 26-MARCH 2, 1982

U.S. FARMERS HOME ADMINISTRATION

The FmHA should give priority to farm ownership and operating loans.

We recommend that the limit on farm ownership loans be increased from $200,000 to $350,000, and operating loans increased from $100,000 to $150,000 as additional funds become available in order not to reduce the number of farms assisted.

We recommend at least $2 billion be made available at reasonable interest rates for operating loans and $2 billion to finance purchases of farms through FmHA for new farmers.

Additional administrative staff should be provided to reduce caseloads when emergency and disaster loans or other unusual programs are initiated. The Administration should be directed to set aside emergency funds to hire temporary staff when emergency situations arise.

We urge continuation of a disaster loan program, administered by the Secretary of Agriculture, and available only to family farmers who have suffered a disaster. Disaster loans should be at low interest rates and have a repayment period of ten years, with deferral of principal up to a period of three years, at the discretion of the FmHA county committee. To prevent future abuses of this program, loans should be limited to the amount of actual loss plus operation adjustment loans not to exceed $100,000.

The Economic Emergency Loan Program, which was instrumental in providing $6.3 billion in loans ince 1978, should be reenacted with another $4 billion in loan authority and should be restricted for use only by family farm operators.

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ATTACHMENT B

Statement of Jim Purcell
President, Farmers State Bank of Hart, Texas
National Farmers Union Fact-Finding Hearing, March 22, 1982
Lubbock, Texas

We are in a unique situation in Hart because it is primarily irrigated country.

This last year we had some 10,000 pound corn (180 bu.) which was not uncommon. The least any of our customers had was 8200 pounds (145 bu.) on the average. We had some two bale cotton.

If you cannot pay back your debt with 10,000 pound corn and two bale cotton, there is something wrong.

Since 1977, the farmer has been betting that this next year is going to be better, that we are going to have record yields, and we are going to have record prices. In our area, we can't control the market on wheat and we have little effect on the cotton due to some of the marketing and manipulation from other sources in the industry. So we have to take what is given.

Bankers in our area look at a source of repayment. This year may be the best year to sell out. At least there are a few buyers. Next year, if things continue, there is not going to be any buyers, so machinery and equipment may be worthless. So repayment is questionable right now.

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ATTACHMENT C

Statement of Bobby Hobgood
American Bank of Commerce, Wolfforth, Texas
National Farmers Union Fact-Finding Hearing, March 22
Lubbock, Texas

I am Bobby Hobgood, American Bank of Commerce, Wolfforth, Texas.

What percentage of farmers are in bad shape? In the Wolfforth area --- and I assume probably it is the same in all the other areas --- somewhere in the neighborhood of seventhy-five to eighty percent are in very bad shape.

From a banking standpoint we look at it in terms of:

If they were to have a farm sale and get out of farming, sell all their equipment --- I am speaking of the tenant farmer now --- they probably would not have enough money to pay out their debts on equipment, operating loans or any other of the disaster loans they may have accumulated over the years.

In our particular area where we are strictly cotton farming, mostly dry land, we have got a serious problem.

This year we had excellent production and still went in the hole. If we do not have an increase in prices, I would estimate than another 30 to 35% of the farmers in our area would not be farming again in 1983. This is alarming.

The sad part to me is that every year there are more and more young farmers getting out of farming and every year the older farmers are retiring and stepping aside. One of these days these older farmers are going to be gone. There is not going to be any younger farmers left. There is going to be a day of reckoning.

ATTACHMENT D

Statement of Ronny Paulger
President, Idalou State Bank, Idalou, Texas
National Farmers Union Fact-Finding Hearing, March 22, 1982
Lubbock, Texas

At the beginning of each year, we, as many bankers, will sit down with our farm borrowers and do a projection based on income and expenses.

In January, 1981, we made our projections based on 58¢ cotton. We made our projections on a group of 21 farms, representing a cross-section of dry land, irrigated and rental farms.

We projected the income (at 58¢) at $2,000,915 for the 21 farms. Operating expense for the same 21 farms was estimated at $1,000,901. This left a net of over $1 million to cover estimated expenses of $714,000, leaving the farm operators with $299,000 after operating expenses and after all debt service.

In October, we did another projection, but this time at about 35¢ a pound. Projected income then was $1,000,878, a drop of one million dollars.

So those 21 farmers went from a $299,999 profit to a $737,000 loss --- that was a million-dollar swing.

We are third and fourth generation farmers, good farmers. For many of them it is the first time they have ever lost money.

If the same thing happens in agriculture in 1982 that happened last year, it would be very questionable to continue to see these people lose their earnings. We would be very unhappy if they decide not to farm again, but in the long run we will be saving them whatever else they have acquired over the many years.

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ATTACHMENT E

Statement of Gary McKellips
Cashier, State Bank of Alcester, Alcester, South Dakota
National Farmers Union Fact-Finding Hearing, March 26, 1982
Sioux Falls, S.D.

We are not in a recession by any means, shape or form --- we are in a depression. We have seen good, efficient operators, who have experienced good crops in 1981, show operating losses in the tens of thousands of dollars. It is almost impossible to construct cash flow statements for our farmers today that have any appreciable amount of debt and come out with a positive cash-flow statement.

The thing that really scares us is the established farmer that can't show a cash flow to meet his indebtedness. We are getting more and more of them. It is safe to say that twenty to thirty per cent of our farmers are in trouble.

And when the Farmers Home is tightening up their purse strings, you have no where to go with them.

ATTACHMENT F

EXCERPTS FROM NFU STATEMENT

TO THE

SUBCOMMITTEE ON CONSERVATION, CREDIT AND
RURAL DEVELOPMENT
COMMITTEE ON AGRICULTURE
U.S. HOUSE OF REPRESENTATIVES

February 4, 1982

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Clearly, the most notable circumstances precipitating the current farm crisis are excessively high interest rates and low commodity prices.

For many farmers and ranchers this year, interest outlays will be their single largest expense item, exceeding even the cost of feed purchases and the cost of purchased livestock.

The outstanding debt of U.S. farmers, which began in 1981, at $82.5 billion, is expected to surpass $200 billion sometime this year. In fact total interest outlays of farmers now equal their net farm income (during the 1960's, interest outlays represented only 16 percent of what net farm income was).

When adding, recent farm commodity prices to the high interest rates factor, agricultures financial picture becomes much more bleak. Low prices have driven net farm income down from $31 billion in 1979 to $19.9 billion in the past two years, and income is projected at $17 billion for 1982. This comprises the three poorest consecutive years since the mid-1950's.

Prices received for all commodities are currently at 56 percent of parity, the lowest level since 1933, a time when farmers endured only two percent inflation.

The aforementioned circumstances, compounded by factors such as the Soviet grain embargo, regionally poor weather and a historically weak farm program are strapping the family farmer, and we are hearing their outcries loud and clear. Our state organizations in North Dakota, South Dakota, Iowa, Colorado and Wyoming have called for a one-year moratorium on FmHA foreclosures. The National Farmers Union has urged Secretary Block to more extensively use his authority in deferring principal and interest payments for farmers facing foreclosure. Please believe us when we say that these are not alarmist reactions but the outpouring of concern stemming from mounting ominous evidence and the first-hand experience of our members.

USDA efforts to downplay farm credit problems by citing only 300 foreclosures for 1981 and indicating that delinqency rates have sharply declined and are being met by astonishment and indignation by those who see a different story unfolding.

In the state of Minnesota alone, their Department of Agriculture cited 304 farm mortgage foreclosures for the year ending February 1, 1981, fully six times the number of foreclosures in the state from the previous year. (This comprised 11 percent of the total farm real estate transfers.) Obviously, since February, the situation has worsened as farmers have seen the value of their 1981 field crops drop by more than $1 billion. Market prices have fallen since May by as much as $1.25 per bushel for soybeans, by almost 90¢ per bushel for corn, by more than 59¢ per bushel for wheat, and by $2.20 per 100 pounds for sunflower seed. Minnesota corn growers alone have experienced a $631 million drop in value for this year's forecast record crop.

One needn't even go beyond USDA statistics to refute the "300 foreclosures for 1981" figure. In a report titled "Farm Program Borrowers In Distress - Month ended November 1981" (see Attachment 1), a state-by-state breakdown shows 2,334 total foreclosures through FmHA with an additional 1,270 bankruptcies. Attachment 2 shows that there were 409 completed or initiated voluntary liquidations for the month of November alone, and reportedly a USDA December report will show 291 involuntary liquidations in that month.

Attachment 2 also indicates that there were 7,528 delinquencies by Farm Program borrowers during November, a continuation in a rising trend which has shown the rate of delinquency on impaired outstanding principal more than tripling in two years, from $501 million to $1.62 billion by September. 1981. That represents an outstanding principal of $11.7 billion, up from $5.5 billion in 1979 and $10.25 billion in September, 1980.

Of that delinquent amount $14.5 million was 30 days or less behind, $374 million was over six months old, and $1 billion in arrears was over one year old.

Attachment 3 indicates delinquent accounts per state as of March 3, 1981. Totaling those accounts, one discovers 105,007 delinquencies or 35 percent of all borrowers. Under Secretary Naylor indicated at a recent press conference that the delinquency rate was down to 15 percent. If, somehow, the 35 percent to 15 percent reduction actually occurred, we would be most interested in how this reduction was accomplished.

In North Dakota, where 30 percent of the 8,200 FmHA loans are delinquent, their state FmHA office is asking 250 to 300 farmers to consider quiting farming this year. Such forms of persuasion do not show up on the foreclosure tally.

Nor are foreclosures the final measure of FmHA efforts being witnessed in Texas. We are informed that there are about 16,000 ownership and operating loans, of which 35 percent are delinquent. FmHA has notified 1,250 farmers that they will no longer continue to be financed and that they could face notice of acceleration and demand for payments. Nine hundred of the 1,250 farmers are located in the panhandle portion of Texas.

The real situation out in the country is not stressful in some regions, as Secretary of Agriculture John Block characterized it at his January 21st press conference, but is one of general depression. We are particularly concerned about the financial vulnerability of the young farmer, who

has not built up the equity to endure extended adversity. Phil Harris, a University of Wisconsin economist, stated in an Associated Press story widely circulated the past few days in Wisconsin that "young farmers in Wisconsin, beset with climbing costs and interest rates can expect to face cash-flow problems that could put many out of farming in coming months."

In the same article, William Saupe, also from the University of Wisconsin, stated that low-equity farmers had to repay an average of $2.37 in debt yearly for every dollar earned from the sale of their products.

Additionally, a University of Wisconsin Extension study of 165 low-equity operations showed that the average financial obligation of the farms exceeded their 1979 income by nearly $11,000.

As we ponder the future of young and old farmers alike, as well as this nation's entire agricultural structure, we know this subcommittee will do all it can to ascertain the facts and untangle the mixed signals that have dominated this issue.

As alluded to in our policy statement,we urge that farm ownership and operating loans be priority programs with the FmHA. We see an immediate need for at least a $2 billion allocation for operating loans, compared to the $1.325 billion allocated in the Omnibus Budget Reconciliation Act of 1981. Additionally, at least $2 billion is needed yearly for farm ownership loans, this compared to the $700 million appropriated in the Budget.

While we recognize the definite need for rural development by means of insuring water and waste disposal loans and community facility loans, this nation is now at the point of deliberating upon the financial fate of thousands of farmers. If they fall, rural development could well be a pointless consideration.

It's important to note that while the budget appropriation for operating loans, $1,325 billion, is up from the 1981 funding level of $875 million, this accomodation was greatly facilitated by the de facto death of the Economic Emergency Loan Program. From early 1979 through June 10, 1981, some 115,823 economic emergency loans were made, totaling $6.3 billion. Obviously, these "freed appropriations" allowed for some redistribution. We do, however, strongly urge the Secretary to use his authority to implement the Economic Emergency Loan Program through September, 1982, and to utilize the full $600 million availed to him.

As you deliberate and significantly impact upon the direction that agricultural policy will quickly turn, it is important to emphasize that what farmers are now experiencing is not a "survival of the fittest" phenomenon, a process by which the unproductive will be needfully weeded out. The vast majority of distressed farmers are efficient and dedicated operators fallen victim to a series of unfortunate circumstances far beyond their control.

Attachment 1

FARMER PROGRAM BORROWERS IN DISTRESS-PRATT EXCEL NOV 1983

| AREA | IN FORECLOSURE (INCLUDES FMHA BORROWERS) | VOLUNTARY LIQUIDATION (INCL. FCRRS) | FILED BANKRUPTCY (INCL. ECPAS) |
|---|---|---|---|
| USA | 478 | 2,334 | 1,270 |
| ALA | 11 | 85 | 25 |
| ARZ | | | 1 |
| ARK | 8 | 57 | 24 |
| CA | 15 | 19 | 17 |
| COL | 7 | 23 | 31 |
| CON | 3 | 10 | 4 |
| DEL | | | 1 |
| FLA | 13 | 117 | 24 |
| GA | 22 | 167 | 75 |
| ID | 18 | 116 | 16 |
| ILL | 10 | 8 | 26 |
| IND | 20 | 71 | 44 |
| IA | 11 | 65 | 20 |
| KAN | 9 | 47 | 26 |
| KEN | 9 | 24 | 45 |
| LA | 2 | 71 | 27 |
| ME | 15 | 25 | 28 |
| MD | 1 | 2 | 1 |
| MAS | 3 | 8 | 2 |
| MI | 6 | 41 | 50 |
| MN | 10 | 28 | 37 |
| MIS | 4 | 104 | 48 |
| MO | 8 | 46 | 42 |
| MT | 4 | 27 | 4 |
| NEB | 25 | 34 | 26 |
| NEV | 1 | 1 | 2 |
| NH | | | |
| NJ | 1 | 16 | 5 |
| NM | 6 | 20 | 5 |
| NY | 13 | 62 | 45 |
| NC | 7 | 111 | 148 |
| ND | 5 | 77 | 19 |
| OH | 12 | 30 | 18 |
| OKL | 21 | 105 | 24 |
| OR | 18 | 83 | 11 |
| PA | 20 | 30 | 42 |
| RI | 1 | | 1 |
| SC | 6 | 101 | 15 |
| SD | 14 | 32 | 27 |
| TEN | 6 | 82 | 56 |
| TX | 11 | 105 | 26 |
| UT | | | 4 |
| VT | 1 | 4 | |
| VA | 13 | 53 | 25 |
| WA | 14 | 51 | 18 |
| WVA | | 8 | 11 |
| WIS | 62 | 144 | 26 |
| WYO | 6 | 1 | 8 |
| ALK | | | |
| HA | | 2 | |
| PR | 2 | 14 | 2 |
| MP | | | |
| VI | | | |

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Attachment 2

SUPPLEMENT MONTHLY FARMER PROGRAM STATUS REPORT FOR THE MONTH OF NOVEMBER

| State | Number of Hours Worked By EM Employees During The Month | | Number of EM and EE Contracts COB | FP Borrowers Who Requested Subordination (OL) During the Month | FP Borrowers Subordinated During The Month | FP Borrowers Who Received Letters During the Month (Servicing Del.) | FP Borrowers That Completed Voluntary Liquidation During The Month | FP Borrowers Voluntarily Liquidated | |
|---|---|---|---|---|---|---|---|---|---|
| | Loan Officers | Clerks | | | | | | By Other Lenders | By FmHA |
| | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 |
| U.S. Total .... | 115,163 | 149,096 | 674 | 2,828 | 2,342 | 7,528 | 288 | 73 | 121 |
| Alabama ..... | 4,455 | 3,305 | 0 | 11 | 6 | 109 | 4 | 3 | 12 |
| Alaska ..... | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Arizona ..... | 152 | 108 | 3 | 1 | 3 | 7 | 2 | 0 | 0 |
| Arkansas ..... | 14,400 | 16,168 | 0 | 304 | 245 | 540 | 8 | 1 | 3 |
| California .... | 1,272 | 1,728 | 25 | 17 | 3 | 128 | 2 | 0 | 0 |
| Colorado ..... | - | - | - | - | - | - | - | - | - |
| Connecticut ... | 0 | 0 | 3 | 0 | 0 | 6 | 0 | 1 | 0 |
| Delaware ..... | - | - | - | 0 | 0 | 1 | - | 0 | 0 |
| Florida ..... | 1,236 | 2,796 | 26 | 27 | 24 | 738 | 7 | 2 | 7 |
| Georgia ..... | 3,736 | 6,623 | 11 | 62 | 4 | 220 | 11 | 13 | 12 |
| Hawaii ..... | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Idaho ..... | 472 | 1,672 | 0 | 137 | 99 | 115 | 4 | 0 | 1 |
| Illinois ..... | 1,106 | 3,946 | 165 | 31 | 12 | 328 | 5 | 2 | 26 |
| Indiana ..... | 0 | 716 | 6 | 7 | 4 | 0 | 6 | 1 | 4 |
| Iowa ..... | 5,623 | 3,585 | 0 | 111 | 101 | 29 | 12 | 0 | 1 |
| Kansas ..... | 706 | 2,329 | 5 | 23 | 26 | 208 | 9 | 2 | 1 |
| Kentucky ..... | 2,868 | 2,653 | 6 | 13 | 13 | 506 | 2 | 0 | 1 |
| Louisiana ..... | 3,956 | 4,869 | 83 | 14 | 15 | 517 | 5 | 0 | 3 |
| Maine ..... | 284 | 690 | 7 | 24 | 23 | 57 | 14 | 0 | 2 |
| Maryland ..... | - | - | 1 | 3 | 3 | 113 | - | 0 | 1 |
| Massachusetts . | 0 | 0 | 0 | 1 | 0 | 7 | 0 | 0 | 0 |
| Michigan ..... | 1,816 | 1,600 | 0 | 45 | 39 | 0 | 2 | 5 | 1 |
| Minnesota ..... | 747 | 1,020 | 3 | 34 | 24 | 68 | 15 | 1 | 0 |
| Mississippi ... | 16,999 | 18,432 | 0 | 91 | 68 | 662 | 9 | 2 | 4 |
| Missouri ..... | 3,316 | 1,020 | 0 | 76 | 63 | 156 | 14 | 5 | 0 |
| Montana ..... | 1,381 | 2,009 | 0 | 41 | 33 | 34 | 5 | 1 | 0 |
| Nebraska ..... | 5,155 | 8,349 | 0 | 22 | 19 | 328 | 4 | 1 | 7 |
| Nevada ..... | 0 | 0 | 0 | 1 | 0 | 0 | 0 | 2 | 3 |
| New Hampshire . | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| New Jersey .... | 791 | 1,137 | 5 | 4 | 7 | 31 | 0 | 1 | 0 |

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Attachment 2a

SUPPLEMENT MONTHLY FARMER PROGRAM STATUS REPORT FOR THE MONTH OF NOVEMBER

| State | Number of Hours Worked By EM Employees During The Month | | Number of EM and EE Contracts COB | FP Borrowers Who Requested Subordination (OL) During the Month | FP Borrowers Subordinated During The Month | FP Borrowers Who Received Letters During the Month (Servicing Del.) | FP Borrowers That Completed Voluntary Liquidation During The Month | FP Borrowers Voluntarily Liquidated | |
|---|---|---|---|---|---|---|---|---|---|
| | Loan Officers | Clerks | | | | | | By Other Lenders | By FmHA |
| | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 |
| New Mexico .... | 68 | 56 | 5 | 4 | 11 | 68 | 0 | 0 | 0 |
| New York ..... | 2,426 | 4,920 | 12 | 45 | 28 | 267 | 28 | 5 | 2 |
| N. Carolina ... | 9,731 | 20,115 | 6 | 48 | 27 | 7 | 22 | 2 | 5 |
| N. Dakota ..... | 5,076 | 5,258 | 1 | 103 | 65 | 418 | 1 | 0 | 0 |
| Ohio ..... | 0 | 298 | 0 | 4 | 3 | 67 | 5 | 1 | 2 |
| Oklahoma ..... | 3,706 | 10,339 | 3 | 38 | 31 | 104 | 6 | 0 | 4 |
| Oregon ..... | 500 | 426 | 2 | 49 | 22 | 413 | 2 | 2 | 0 |
| Pennsylvania .. | 536 | 1,052 | 0 | 18 | 12 | 76 | 10 | 2 | 1 |
| Rhode Island .. | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| S. Carolina ... | 1,655 | 2,521 | 21 | 7 | 3 | 71 | 6 | 0 | 0 |
| S. Dakota ..... | 982 | 1,415 | 26 | 455 | 430 | 286 | 16 | 4 | 1 |
| Tennessee ..... | 2,991 | 2,885 | 0 | 9 | 5 | 156 | 4 | 0 | 6 |
| Texas ..... | 8,261 | 10,326 | 0 | 797 | 743 | 261 | 21 | 1 | 0 |
| Utah ..... | 0 | 0 | 0 | 30 | 20 | 0 | 1 | 1 | 0 |
| Vermont ..... | 0 | 0 | 0 | 0 | 0 | 0 | 1 | 0 | 0 |
| Virginia ..... | 4,340 | 1,181 | 0 | 7 | 5 | 166 | 5 | 1 | 5 |
| Washington .... | 0 | 1,154 | 0 | 56 | 57 | 25 | 2 | 0 | 2 |
| W. Virginia ... | 0 | 0 | 0 | 0 | 0 | 0 | 2 | 1 | 3 |
| Wisconsin ..... | 4,420 | 2,395 | 249 | 40 | 29 | 233 | 13 | 7 | 0 |
| Wyoming ..... | 0 | 0 | 0 | 18 | 17 | 0 | 1 | 0 | 0 |
| Puerto Rico ... | 0 | 0 | 0 | 0 | 0 | 2 | 2 | 1 | 1 |
| Virgin Isl. ... | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| W. P. Terr. ... | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |

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FmHA Farm Loan Delinquency Reduction Goals* Attachment 3

| State | Delinquent Accounts** March 31, 1981 | Delinquency Goal for March 31, 1982 | Delinquent Accounts to Be Eliminated | Percentage Reduction |
|---|---|---|---|---|
| Alabama | 3,714 | 2,840 | 874 | 23.5% |
| Alaska | 21 | 15 | 6 | 28.6% |
| Arizona | 857 | 646 | 211 | 24.6% |
| Arkansas | 4,068 | 3,108 | 960 | 23.6% |
| California | 1,296 | 991 | 306 | 23.6% |
| Colorado | 1,347 | 1,036 | 311 | 23.0% |
| Connecticut | 118 | 90 | 28 | 23.7% |
| Deleware | 109 | 83 | 26 | 23.9% |
| Florida | 2,692 | 2,057 | 635 | 23.6% |
| Georgia | 6,657 | 5,066 | 1,501 | 22.9% |
| Hawaii | 91 | 66 | 25 | 27.5% |
| Idaho | 2,668 | 2,018 | 650 | 24.4% |
| Illincis | 2,499 | 1,908 | 591 | 23.6% |
| Indiana | 1,860 | 1,426 | 434 | 23.3% |
| Iowa | 2,146 | 1,653 | 493 | 23.0% |
| Kansas | 2,046 | 1,556 | 490 | 23.9% |
| Kentucky | 2,604 | 1,995 | 609 | 23.4% |
| Louisiana | 3,146 | 2,394 | 752 | 23.9% |
| Maine | 1,748 | 1,298 | 450 | 25.7% |
| Maryland | 322 | 246 | 76 | 23.6% |
| Massachusetts | 143 | 109 | 34 | 23.8% |
| Michigan | 2,344 | 1,790 | 554 | 23.6% |
| Minnesota | 3,673 | 2,833 | 840 | 22.9% |
| Mississippi | 5,904 | 4,519 | 1,385 | 23.5% |
| Missouri | 4,144 | 3,126 | 1,018 | 24.6% |
| Montana | 1,094 | 834 | 260 | 23.8% |
| Nebraska | 2,889 | 2,221 | 668 | 23.1% |
| Nevada | 181 | 121 | 40 | 24.8% |
| New Hampshire | 42 | 31 | 11 | 26.2% |
| New Jersey | 560 | 417 | 143 | 25.6% |
| New Mexico | 879 | 660 | 219 | 24.9% |
| New York | 1,778 | 1,358 | 420 | 23.6% |
| North Carolina | 4,628 | 3,556 | 1,072 | 23.1% |
| North Dakota | 3,126 | 2,422 | 704 | 22.5% |
| Ohio | 986 | 751 | 235 | 23.8% |
| Oklahoma | 3,980 | 3,032 | 948 | 23.8% |
| Oregon | 853 | 643 | 210 | 24.6% |
| Pennsylvania | 1,154 | 870 | 284 | 24.6% |
| Rhode Island | 16 | 11 | 5 | 31.3% |
| South Carolina | 2,189 | 1,670 | 519 | 23.7% |
| South Dakota | 3,715 | 2,898 | 817 | 22.0% |
| Tennessee | 3,253 | 2,483 | 770 | 23.7% |
| Texas | 9,898 | 7,539 | 2,359 | 23.8% |
| Utah | 256 | 192 | 62 | 24.4% |
| Vermont | 218 | 161 | 57 | 26.1% |
| Virginia | 3,192 | 2,459 | 733 | 23.0% |
| Washington | 953 | 727 | 226 | 23.7% |
| West Virginia | 485 | 349 | 136 | 28.0% |
| Wisconsin | 1,850 | 1,424 | 426 | 23.0% |
| Wyoming | 615 | 470 | 145 | 23.6% |

* Based on FmHA AN No. 580 (1900), August 25, 1981.
** Total for all farm loan types (Farm Ownership, Soil and Water, Operating, Emergency, Economic Emergency).

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[The following material was inserted by Mr. Hall, see p. 71 for oral reference.]

**APPENDIX**

**to**

**Statement of the Water Quality Association**

**on**

**S. 2314**

**Senate Subcommittee on Agricultural Credit and Rural Electrification**

**April 21, 1982**

## THE WATER QUALITY ASSOCIATION, HISTORY & ACTIVITIES

The Water Quality Association (WQA) is an international trade association of some 1,400 member firms and individuals engaged in the design, manufacture, production, distribution and sale of equipment, products, supplies, and services for producing quality water for specific uses in residential, commercial, industrial and institutional establishments. WQA is a nonprofit organization, the objectives of which are promotion of water quality improvement technology, facilitation of information exchange, conduct of educational and community affairs programs, publication of materials relating to the quality of water, plus other functions of traditional trade association nature intended to benefit the public through industry betterment.

WQA is the result of a merger of two associations in 1974. Together the Water Conditioning Association International and the Water Conditioning Foundation served the Industry from 1945 and 1948, respectively. In addition, the WQA headquarters houses and provides management services to two additional corporations.

The first is the Water Quality Research Council (WQRC). This organization enjoys charitable tax status and is eligible to receive grants from government and private foundations. This Council has funded research on topics such as corrosion, water quality and animal health, soft water beneifts, the effects of waste discharges on aerobic and anerobic septic systems, a study of the significance and control of bacteria in water filters and plumbing systems, and a study on energy savings in water heaters with soft water. WQRC has also sponsored a series of seven international water quality symposiums.

The second organization for which WQA has provided management services is the Water Quality Improvement Standards and Certification Council (Council). This Council was formed in July 1976, and recently became inactive upon completion of its mission. The founding members included manufacturers of water filters, bacteriostatic water treatment units and water purifiers as well as representatives of the National Sanitation Foundation, American Bottled Water Association, The Silver Institute and Water Quality Association. The spark for the Council's creation was provided by the Federal Environmental Protection Agency's very active interest in what was loosely referred to as "home water treatment units." The Council dealt

with technical problems, standards writing, labeling and misbranding, and information and education. Since its founding, a major goal of the Water Quality Improvement Standards and Certification Council, was the development of a voluntary standard covering water treatment units and systems used in the improvement of water for human consumption.

## THE POINT-OF-USE WATER TREATMENT INDUSTRY

The Point-of-Use Water Treatment Industry is an Industry whose business is improving the quality of water used in our homes, institutions, and business enterprises, and it improves the quality most economically at the point where it is needed and only the quantity required. The Industry provides treatment service anywhere from a single faucet to small communities and everything in between.

According to a survey commissioned by WQA, Ernst & Whinney reports that we are an Industry of over 200 manufacturers, nearly 5,000 retailers, distributors, wholesalers, and nearly $1 billion in annual sales. It is an Industry employing over 50,000 men and women, serving more than 5 million families, and more than ½ million commercial/industrial/institutional customers.

## INDUSTRY PRODUCTS & THEIR APPLICATION

The Point-of-Use Water Treatment Industry has developed a variety of methods for improving water at the point of use. They include:

**Filtration** -- to remove turbidity, certain types of color and other particulate matter. Removes dirt particles to a rated micron size. This process is used in homes and the food and beverage industries, and wherever an improved water quality is desired for drinking, cooking, ice-making, and so forth. Special microfiltration devices which can remove bacteria are also available.

**Adsorption** -- the process in which matter adheres to the surface of an adsorbent. An adsorbent is a material, usually solid, capable of holding gases, liquids and/or suspended matter at its surface and in exposed pores. Activated carbon is a common adsorbent used in water treatment which removes chlorine taste, certain organics, and musty and fishy odors. Fluoride removal with activated alumina is a special application of adsorption.

**Deionization** -- to produce water virtually free of minerals to less than 1 mg/l required in high pressure boilers, metal plating, electronics manufacture, jet engine operation, ice-making, and so forth. Deionization (DI) is often used as part of a purification system which prepares water for use in pharmaceuticals, injection into the body, hemodialysis, and wherever water of extremely high quality is difficult or impossible to improve by other processes. This process also removes nitrates and sulfates.

**Distillation** -- the process in which water is converted into its vapor state by heating, and the vapor cooled and condensed to the liquid state and collected. Used to remove solids and other impurities from water.

**Reverse Osmosis** -- used to remove substantially all suspended or dissolved matter from water. A process in which pressure is used to force water through a semi-permeable membrane which will transmit the water but reject most other dissolved ions. Reverse osmosis (RO) may be used alone or as part of a system to prepare water of extremely high quality.

**Disinfection** -- there are a variety of methods for disinfecting water at the point of use. These include:

**Chlorination** -- a chlorinator or chemical feed pump is a mechanical device specifically designed to feed chlorine gas or solutions of its compounds, such as hypochlorites, into a water supply in proportion to the flow of water.

**Ultraviolet** -- a method of water disinfection which employs ultraviolet light to destroy water borne bacteria. Sometimes used in conjunction with other disinfection methods to maintain bacterial quality during storage.

**Ozonation** -- Ozone ($O_3$), an unstable form of oxygen and a strong oxidizing agent, is being used as a disinfectant for water.

**Iodination** -- disinfection method recommended for transient populations and for temporary disinfection.

**Bromination** -- a disinfection method where bromine is released from impregnated resin cartridges; now used in marine and off-shore applications.

**Silver Bacteriostasis** -- a method which inhibits bacteriological growth through oligodynamic means.

**Oxidation** -- the action of an oxidant for precipitating and removing water impurities such as iron, manganese, hydrogen sulfide, and many organics.

**Neutralization** -- the addition of either an acid or a base as required to produce a neutral solution. The use of alkaline or basic granular materials to neutralize the acidity of some water is a common practice at the point of use.

**Cation Exchange Softening** -- removes calcium and magnesium, two minerals which seriously impair water's cleaning capabilities and which can deposit a damaging scale in boilers, heaters, plumbing pipes, fixtures, and water-using appliances. Besides its use in homes, where it is essential for bathing, personal grooming, and cleaning, softened water is required by commercial laundries, car washes, restaurants, dairies, beauty salons, and in

manufacturing processes such as textile manufacture and those involving steam production. Reduces hardness to less than 17 mg/l and may remove iron, manganese, and other cationic heavy metals depending on their concentrations, to levels below proposed Federal Secondary Regulations. Also removes 90-97% cationic radioactivity.

**Chemical Treatment** -- a process often used for controlling corrosion which is the destructive disintegration of a metal by electrochemical means. Usually involves the feeding of polyphosphates and/or silicates with a chemical feed pump.

**Electrodialysis** -- a process in which a direct current is applied to a cell to draw charged ions through ion selective semipermeable membranes, thus removing the ions from the solution.

**Combinations of Methods** -- in many cases, combinations of the basic methods are used to solve water quality problems. For example, chlorination may be used for disinfection and the precipitation of iron or hydrogen sulfide, which then is removed by filtration. Activated carbon is often used in combination with reverse osmosis treatment to remove low molecular weight organic compounds that pass through the RO membranes.

All of the aforementioned products and processes may be applied at the point-of-use in a variety of ways. This range of alternatives includes a single faucet, selected water lines, full household, and countertop batch process.

Likewise, the range of cost varies, and most products are available for outright sale or for rental from one of thousands of water treatment professionals in our Industry. Rental prices for individual household treatment methods range from $5 to $15 per month, and individual product prices for outright sale from $10 to $1,600.

Finally, the range of effectiveness, or quality of treated water, also covers a broad spectrum.

For example, each of the five disinfection methods—chlorination, ultraviolet, ozonation, iodination and bromination—meet the bacteriological requirements of the Federal Interim Primary Drinking Water Regulations. Filtration at the single faucet may remove dirt particles to a rated micron size of 300 microns to below 1 micron, and full household filtration from 50 microns to 1 micron. Asbestos can be removed to undetectable levels with reverse osmosis or fine filtration. Lead, cadmium and similar heavy metals are reduced by carbon and removed to extremely low levels by ion exchange softening, reverse osmosis, deionization, distillation, and electrodialysis. There are products now on the market capable of removing trihalomethanes to a level below EPA's proposed maximum contaminant level—these include properly designed carbon units and reverse osmosis plus carbon units.

The Point-of-Use Water Treatment Industry is thus capable of, and does fill a need with treatment technologies that exist almost across the whole board, throughout the entire spectrum of possible requirements.

## POINT-OF-USE POTENTIAL: SMALL COMMUNITIES, PRIVATE WATER SUPPLIES, NON-COMMUNITY WATER SUPPLIES

The Point-of-Use Water Treatment Industry has developed new technology that can dramatically increase our capability of economically serving the needs of small water systems.

Most everyone is aware that small water systems have an extremely serious cost problem in meeting the primary drinking water standards. The problem, of course, is the requirement of large capital investment in equipment with high operating costs. In addition, the need for trained operating personnel plagues almost every community.

Meeting today's primary standards with yesterday's technology and concepts of central water treatment is just not cost-effective.

In examining the extent of this problem, it becomes apparent that there are three categories of concern. The first area of concern is community water systems. The surprising thing to many is that the overwhelming majority of community water systems are quite small:

| | | |
|---|---|---|
| 25 to 500 people | - | 18,022 or 52% of all systems |
| Under 2,500 people | - | 27,804 or 80% of all systems |
| Under 10,000 people | - | 31,946 or 92% of all systems |

The second area of concern is the millions of homes on private water supplies. These are truly small water systems—about 10 million residences served by private wells—a segment that is growing by 500,000 private wells a year according to the National Water Well Association. These are permanent homes, second homes, or vacation homes—millions of Americans who cannot be forgotten, although they are not covered by the Safe Drinking Water Act. They are just as concerned however, if not more so, about the quality of the water that they drink.

The third area of concern is the 250,000 non-community water supplies that serve 25 to 30 million Americans. These supplies are, of course, covered by the Primary Drinking Water Act.

Fortunately, our Industry now has the capability, through new water treatment technology and through the standardization of equipment components, to manufacture small packaged systems to correct problems from a specific source of drinking water on a cost-effective basis. And these systems are available today—we don't have to wait until 1985 or 1990.

The biggest problem is the reluctance of the water supply industry and regulatory agencies to accept change.

It has been said in the scientific community, "Don't forget that for any new idea, there are three phases that you have to go through. First, people will abhor the idea; then they will tolerate it; and finally, they will embrace it." Our only objective should be to achieve high quality drinking water at the lowest cost. We should not restrict new technology, but allow the results of research and development of manufacturers, consulting engineers, and governmental agencies to make available new systems without unnecessary restrictions.

These new packaged filtration systems are very dependable and cost-effective. They are ideal for smaller communities, for private water supplies, and for non-community water supplies.

Consideration of the conventional water filtration plant used by large cities reveals that they involve the mixing of chemicals, flocculation basins, sedimentation basins, and huge gravity filtration beds.

By comparison, the new technology results in a small packaged system that is a completely pressurized, closed, filtration system. Water is pumped to a centrifugal separator, a contact clarifier, and a multimedia filter. The resulting water quality is well below 1 NTU which is so important to adequate disinfection. This type of equipment requires little attention by the operator, low capital investment, and low operating costs.

Looking a little more carefully at packaged system components reveals that the centrifugal separator is used instead of settling basins, removing larger particles down to 75 microns with automatic blowdown; then a polymer feed to form a floc to a pressure contact clarifier, where clarification is obtained in five minutes instead of the normal two to four hours; then to a multimedia filter, where filtration occurs completely throughout the bed. All of these are operated under pressure, and this new system reduces waters of 100 to 200 NTU down to below 1 NTU.

Iowa State University filtration tests at the Gilbert, Iowa, treatment plant compared turbidity and iron removal effectiveness of a conventional sand filter versus a new type of multimedia filter. The multimedia filter produced water which was consistently within state requirements. And the service cycle was typically three to four times longer than the single-layer sand filter, even though the multimedia filter was operated at rates up to 7½ gpm per square foot of filtering media.

Another phase of the filtration study was conducted at the Iowa City treatment plant. The conventional treatment plant was compared with a new chemical feed system followed by direct filtration equipment which required only eight minutes of process time. The direct filtration equipment consistently produced water of equal or better quality than the conventional plant, even though it was operated at rates of about 7 gpm per square foot.

One set of tests showed that 31 NTU surface water was typically reduced to 0.6 NTU by direct filtration operating at 7½ gpm per square foot.

## COST COMPARISONS

Cost comparisons are also important. In the publication, "State Of The Art Of Small Water Treatment Systems," published by the EPA in August 1977, and reviewed by Black and Veatch, custom versus prefabricated modular systems were evaluated. The first example was the conventional custom system with a capacity of 300,000 gallons per day which could serve a small community of 2,000 to 3,000 people. A capital investment of $454,500 is required for equipment, not counting the land or building. Using a capital recovery factor of 30 years at 8%, you would have an annual capital cost of $40,370 plus a yearly operating cost of $70,355, or a total of $110,725 per year. If this were a small town of 2,000 people with even 600 connections, this would result in $185 per year per connection for filtration alone, or $1.01 per thousand gallons.

Another example used was a packaged conventional water filtration system using the same processes with a capital investment of $209,000. Although this example also amortized the capital over a 30-year period, we believe it is more realistic to use a 20-year period. This results in an annual capital cost of $21,290 plus $12,900 for operating costs . . . a total of $34,190 per year which is $57 per subscriber, or 31¢ per thousand gallons.

If conventional settling tanks are replaced by centrifugal separators and open clarifiers are replaced by contact clarifiers and the single media filters are replaced by a high rate multimedia filter system, this initial investment can be reduced from $454,500 for the custom engineered plant to $154,000. This is 66% lower. And instead of the $209,000 investment for the prefabricated packaged conventional plant, the cost of only $154,000 is 26% less, allowing a municipality to produce safe drinking water for only $47 per subscriber, or 27¢ per thousand gallons.

In short, new technology in one type of pre-engineered packaged system allows small municipalities to comply with EPA regulations because they can now afford to comply.

## OPERATIONS

There are serious problems in operating water treatment plants. Here again, our Industry has resources and can help. Every small community cannot expect to have a full-time qualified water treatment specialist. One of the subjects discussed at EPA's Small Systems Symposium last November was the circuit rider concept.

What can be done to serve the 30,000 communities that need help? From an Industry viewpoint, there are approximately 3,000 full-time water conditioning and water treatment dealers in America.

These people could be qualified by our Association, the Water Quality Association, with our personnel certification program. As of 1981, almost two-thirds of the WQA membership have successfully participated in the examinations leading to certification under our voluntary certification programs. In 1981 alone, 798 examinations were administered under these programs.

## ECONOMICS OF POINT-OF-USE TREATMENT

Out of the present total community water use of 175 gallons per capita per day, less than two gallons per capita per day is used for drinking and cooking. The other 173 gallons per capita are used for purposes such as sprinkling lawns, flushing toilets, irrigation, fighting fires, cleaning streets, laundry, bathing, and industrial uses. This means that to meet the EPA drinking water regulations, 99% of water supplied by communities will be purified to a higher quality level than necessary.

Does this always make economic sense? What is going to be the per capita cost of improvements needed in small communities to comply with Federal regulations? Might not an alternative be more economical than a central system? At the community level, for example, one Ohio town, West Liberty, with 645 connections actually considered free distribution of point-of-use units to each household rather than make $923,000 worth of improvements to its central treatment plant. This is an indication that point-of-use treatment technology is a viable alternative to central treatment plants.

If consumers in Boston want lead removed from their water, it can be done now.

If consumers in Nevada want arsenic removed from their water, it can be done now.

If consumers in Illinois, Iowa, or Pennsylvania want radioactivity removed from their water, it can be done now.

With these point-of-use capabilities, why a en't they more widely used? Why aren't we moving ahead? What is stopping us from our efforts in supplying better water to consumers? The answer is found in certain barriers--barriers arising out of lack of Federal recognition that point-of-use water treatment is a viable, workable, existing and often a less costly alternative. This in turn creates another barrier—a barrier to investment.

In the present situation, even if an industrial company goes ahead, does the research, does the design work, and builds the equipment, it has no assurance that the Government rules are not going to change and put it out of business. Until the situation is clarified, the private sector, depending as it must on investor input, cannot do the job of which it is capable. As a result, public attention and public policy are focused entirely--and in many cases to

the consumer's disadvantage—on central water treatment as the only way to go.

## GRADES OF WATER

Thus is described the present state of the art in this Industry--without bond issues, without huge construction projects, without delay, without obsolescene--available to consumers today. Point-of-use treatment has the potential for providing or treating water to meet all requirements of both the interim Primary and proposed Secondary Drinking Water Regulations. This alternative can provide water for private systems, small community supplies, non-community supplies and for those persons needing special water--water for illness or during different periods of life, such as nitrate-free water in infancy. Most important, only that water which needs to be of drinking water quality is treated to that quality.

As previously indicated, many consumers have three qualities of water today. Central treatment and the Point-of-Use Water Treatment Industry are presently working together to provide the best quality water for their specific uses. Consumers, thus, have a disinfected "utility grade" water which they use for fire fighting, sprinkling, and other uses where optimum drinking water quality is not essential. They also have a "working grade" water which is softened in the home and used for laundry and bathing. And, finally, they have an "optimum grade" water highly purified at the point-of-use to supply that 1% used for drinking and cooking.

## GOVERNMENT

The Water Quality Association thus urges avoidance of single-method, single-minded government regulation in the national goal attainment mechanism. In this respect, we would support legislation which would condition future regulation on the use of flexibility, cost-benefit justification, and reasonableness.

Our Association and its members are of the judgment that the governmental process should be based on at least the following general principles: Decisions must be based on adequate information concerning the need for and consequences of proposed action. Action should be undertaken only when there has been a convincing demonstration that potential benefits to society outweigh potential costs. Net benefits to society should be maximized. The existence and utility of all available alternative approaches to any given regulatory objective should be fully explored, and the one producing the least net cost to society adopted. Regulatory priorities should be determined in such manner as to maximize the aggregate net benefits, taking into account industrial, economic, and all other conditions which are significant to the promotion of the general welfare and attainment of every broad national objective.

We are confident that the employment of such principles will be productive of point-of-use water treatment technology as an acceptable and, in many cases, preferable alternative method of providing safe drinking water.

[The following press release was submitted by Bruce Workman; see p. 74 for oral reference.]

IOWA STATE UNIVERSITY,
*Ames, Iowa, April 19, 1982.*

[Press Release]

CONCERN OVER FUTURE OF RURAL WATER SYSTEMS

AMES, IOWA.—A newly released research report on rural water systems in five Midwestern states raises concerns about their current administration and financial future.

Research estimates indicate that many of the systems examined in the study were behind in their debt service payments. The study also reported that many rural water system record and accounting systems did not provide adequate information for financial analysis and management.

Paul H. Gessaman, professor of agricultural economics at the University of Nebraska-Lincoln, and Teresa N. Janovec, a research technologist at the same school, worked with data supplied by 26 rural water systems in Iowa, Missouri, Nebraska, North Dakota, and South Dakota. The 26 systems were selected as a sample of the 108 systems in the study.

Entitled "Operational Characteristics of Rural Water Systems in Five North Central States," the report is based on research funded jointly by the North Central Regional Center for Rural Development at Iowa State University; the Agricultural Experiment Stations of Iowa, Missouri, Nebraska, North Dakota and South Dakota; and the Economic Research Service of the U.S. Department of Agriculture.

All the water systems examined were financed under the Farmers Home Administration (FmHA) Water and Waste Disposal System program and were constructed between 1970 and 1977.

The report is critical of recordkeeping by the FmHA and the rural water system governing units. "It appears that FmHA records are not adequate to consistently establish: (1) the actual capital cost of a rural water system, (2) the actual per-user and total financial contributions made by water users, (3) the current status of debt service payments made by a rural water system, and (4) the number and type of water users who secure water from a rural water system," the report states.

Estimates indicated that 14 of 20 systems providing complete financial data had total deficits on debt service payments of $766,907, an average of $54,779 per system. Some are nearly 50 percent behind in their debt service. The six systems with payments that were more than current were estimated to be ahead by about $64,932, an average of $10,882 per system.

Among the 20 systems, all seven with less than 300 regular water users were estimated to be behind on their debt service payments.

The research revealed that debt service loads for some systems are heavy and vary from system to system. The average debt service per water user for servicing FmHA debt was estimated to be $167 per year. One system reported having a debt that would require an estimated debt service of $420 per water user per year.

In order to meet debt service payments, water rates would have to be increased substantially for some systems. However, if use of water decreased significantly due to a rate increase, a system's revenues could decline, leaving it in greater financial difficulty than before the rate increase. "For some systems there are no easy answers to revenue shortfalls," Gessaman says.

"We believe the water systems examined in this research are reasonably representative of systems in the five states," Gessaman says.

Gessaman projects that some of the rural water systems in the Midwest "will experience severe financial pressure" in the future.

"Proposed budget cuts and the recently increased interest rates for water system loans could result in greatly reduced rural water system construction in the next few years," Gessaman says.

The report is the first of three research reports focused on rural water systems constructed between 1970 and 1977 in the five North Central states. The other two reports are intended to help rural residents evaluate their water supply alternatives and to identify external effects of systems such as water system effects on land use and local property taxes.

Copies of the report may be obtained free by writing the North Central Regional Center for Rural Development at 108 Curtiss Hall, Iowa State University, Ames, Iowa 50011.

STATEMENT OF NORMAN DEWEAVER, AD HOC TASK FORCE ON RURAL WATER SEWER PROGRAM REFORM

My name is Norman DeWeaver. I have the privilege of appearing before the Committee on behalf of an informal national network of organizations involved in the development of water supply and waste disposal facilities in small, low income rural communities.

Several of the field groups participating in this network are represented on the panel with me. Ms. Holly Leach of the Water Resource Assistance Corporation is active in solving water and wastewater problems in small communities in eastern Kentucky. Mr. Harvey Johnson heads the Mississippi Institute for Small Towns, an organization that has worked directly with municipal officials in some of the poorest rural communities in his state in addressing their water and waste disposal problems. Mr. Ken Bruzelius heads the Midwest Assistance Program, a technical assistance organization active in the Great Plains states, including Nebraska.

The experience of all our groups, and others like us serving other areas of the country, demonstrates the central role which the grant and loan programs of the Farmers Home Administration play in bringing a reliable supply of potable water and providing for the sanitary disposal of wastewater, at affordable rates, to many tens of thousands of rural households.

We strongly support a multi-year extension of the legislative authorization for the FmHA water and waste disposal loan program. As my associates will attest from their local experience, there is still a job to be done.

Yet simply extending the existing FmHA programs is not enough. Changes in the law are needed. Over the last year, the amount of assistance available to rural communities for the construction of water and wastewater facilities has declined precipitously. The roughly 50 percent cut in program levels for FmHA water-sewer assistance, compounded by cuts in other programs that formerly addressed similar needs, has produced a backlog of formal funding requests equal to more that five years' of appropriations at current levels. Making fair and equitable decisions on which communities should receive the limited assistance available has become an urgent matter. At the same time, the interest rate for most FmHA water-sewer loans has gone from a flat 5 percent for all communities to over 12 percent for most communities. What little assistance Farmers Home has is simply unaffordable for many small towns that need help the worst.

This Committee, along with your counterpart in the House, realized that changes in the program would have to be made to meet current conditions. The Report of the conferees on last year's Reconciliation Act and, later last year, on the farm bill, called on FmHA to target grant and loan assistance better and to institute a project selection system to insure that those needing the help worst got it first.

Farmers Home has not made these changes. Its recently proposed changes in regulations do not meet the standards set in the Conference Committee Reports on the Reconciliation Act and the farm bill. Your committee and the Congress as a whole must take legislative action to make the programs workable under the present difficult circumstances.

Changes are most urgently needed in five areas.

1. A GRADUATED SET OF INTEREST RATES

When Congress authorized FmHA to increase the interest rate for water-sewer loan program, it clearly indicated that it expected the agency to vary the rate based on a community's ability to pay. Instead, Farmers Home increased the rate on nearly all its loans to nearly two-and-a-half times the previous 5 percent rate. Eighty-nine percent of the fiscal year 1982 funds which the agency lent through March 15 were lent at the full market rate. Current regulations provide for only one rate below market, a 5 percent rate for communities where more than half the population have incomes below the poverty level.

After months of prodding by members of Congress, FmHA has just recently issued proposed rules which would establish a so-called intermediate rate—a percentage half way between 5 percent and the market rate—for projects in communities with incomes less than 85 percent of the statewide non-metropolitan median family income level. Not only does this proposal fail to meet the intention of Congress as expressed in the Conference Committee report on the farm bill; it introduces a brand new set of inequities into the program, while still putting the program out of the financial reach of many low income communities.

The new inequities stem from the fact that there is considerable variation between the poverty level figure, a national level of $8450, which FmHA would continue to use to establish eligibility for 5 percent loan money, and the state-specific

standard of 85 percent of non-metro median family income. In Mississippi, these levels are only $1,200 apart while in Connecticut they are almost $10,000 apart. This means that many communities in Connecticut would qualify for the intermediate rate (about 9 percent under current conditions), while few in Mississippi could qualify.

We urge the Committee to amend the reauthorization bill, S. 2314, to require a graduated set of interest rates, with a 5 percent rate established for all communities whose income is less than 80 percent of the statewide non-metro median and which have health problems caused by inadequate water supply or wastewater collection and treatment facilities. Further, a rate of not more than 7 percent should be established for other communities whose income is not more than 100 percent of the statewide non-metro median.

### 2. A GRANT RATE FORMULA BASED ON COMMUNITY INCOME AND SIZE

Farmers Home currently uses two separate administrative rules to determine the amount of grant support, or the grant rate, it will apply to each project requesting grant assistance. The interpretation of one rule, the "similar community" rule, is completely subjective. It says that FmHA will not consider grant assistance unless a system has rates for its water or sewer service that are at least as high as "similar" communities. The second rule, the so-called 1 percent rule, pegs that grant rate to the relationship between the system's debt service for facilities construction and the community's income. Application of the rule is also susceptible to varying interpretations. FmHA now proposes to add a third administrative rule, a provision that no community can receive grant assistance if its income level exceeds 85 percent of the statewide non-metro median.

This thicket of rules fails to accomplish its targeting purpose. It is confusing. It produces strange results, such as diverting grant funds to subsidize market interest rates for FmHA loan funds. Although the grant funds are to be used to help make projects financially feasible in the poorest communities, by March 15 only 5 percent of the fiscal year 1982 grant funds were awarded in conjunction with fiscal year 1982 5 percent loans—loans which under the current regulations should have gone to projects in poverty level communities.

We urge the Committee to amend the reauthorization bill to require that the grant rate for each project be determined by a formula based solely on community income level and size—the two factors most directly related to ability to pay. Further, the formula should insure that communities whose income is less than 80 percent of the statewide non-metro median and whose population is less than 1,500 should be entitled to the maximum grant rate.

### 3. IMPLEMENTATION OF A PROJECT SELECTION SYSTEM

As both grant and loan funding for the FmHA water-sewer programs has shrunk, the size of the backlog of unfunded requests for assistance has ballooned. At current appropriations levels, it would take the agency over five years just to deal with the existing backlog.

Farmers Home has no system to objectively compare competing requests for assistance, no way to insure that the most needy projects get what little assistance is available. This situation exists even though the agency has many priorities, and is about to add another—a priority for "truly rural" communities. FmHA has no way of weighing one priority against another.

Congress has asked FmHA, not once, but twice in the last year to institute a project selection system. Farmers Home has not even published proposed regulations to meet this need.

We urge the Committee to amend the reauthorization bill to require a project selection system which incorporates three basic factors—community size, income and severity of health need—as a means of deciding which projects get the funds available and which don't.

### 4. AUTHORIZATION FOR A TECHNICAL ASSISTANCE PROGRAM

At present, Farmers Home has only one means of responding to a community that has water supply or waste disposal problems—to fund the construction of new facilities. Most communities have only one source to turn to for advice—engineering firms whose reimbursement for services is frequently contingent on FmHA approval of a project and whose fees increase as the cost of the project increases.

There is no economically disinterested third party to help the community. If its problems could be addressed through a non-construction alternative, like a water

conservation program, neither FmHA nor the engineering firm has any reason to be interested.

Experience with a number of groups, such as those represented by my associates on the panel, shows that there can and should be another approach to this situation—technical assistance organizations that can provide rural communities with disinterested advice on the most cost-efficient way to solve their water supply and waste disposal problems.

We urge the Committee to amend the reauthorization bill to authorize the funding of nonprofit technical assistance centers and the earmarking of a small portion of FmHA water-sewer grant program funds for this purpose.

#### 5. ESTABLISHMENT OF A PREDEVELOPMENT FUND

The changes we are suggesting are intended to insure that the rural communities with the most severe problems are the ones that have the first claim on available FmHA resources. Yet all of the items we have recommended to this point would still not help the community that has a major technical problem it must resolve before applying for FmHA loan or grant assistance.

There should be a way of reaching communities with predevelopment needs, such as the need to drill a test well or the need to carefully investigate which of two alternative approaches to its problems may be most cost-efficient. Again, my associates have been involved with pilot projects extending grant and loan support to communities with such needs. The results have proven the effectiveness of such predevelopment funding.

We urge the Committee to amend the reauthorization bill to authorize a predevelopment fund for communities with technical problems which must be solved before they can compete for FmHA assistance.

All five of these recommendations go together. They insure that the Congressional intent, expressed in the Conference Committee Reports on the Reconciliation Act and farm bill, will be met. They insure, in simple, predictable ways, that what grant and loan funds are available are used for communities whose needs are most severe. They promote cost-effectiveness through changes in the grant rate rules, as well as the creation of technical assistance and predevelopment fund programs. All of these recommendations found unanimous bipartisan support in the action taken to date by your counterpart Subcommittee in the House of Representatives.

We urge you to add these features to the pending bill.

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### STATEMENT OF KENNETH BRUZELIUS, EXECUTIVE DIRECTOR, MIDWEST ASSISTANCE PROGRAM, INC., NEW PRAGUE, MINN.

My name is Kenneth Bruzelius. In my capacity as Exectuive Director of the Midwest Assistance Program, a multi-state rural technical assistance agency, I have the opportunity to be aware of the difficulty that many rural communities face as they seek to resolve very pressing water and wastewater problems.

None of the nine midwestern states within the service area of the Midwest Assistance Program are exempt from these problems. The problems vary from community to community, some examples being:

#### GOODRIDGE, MINN.

This northern Minnesota community of about 200 residents, the majority of which are elderly, has an inadequate water system, according to the Minnesota Department of Health, and has no communal wastewater system. With very high groundwater, their septic systems fail creating a potential health problem.

Three (3) years ago they presented a funding request to the Farmers Home Administration. After holding the application about two years, Farmers Home returned it with an indication that the community was too poor for a loan and adequate grant funds were not available.

I believe if the Farmers Home Administration had an adequate project selection system, communities needing their assistance would know on an annual basis where they stood in the selection process. Also, if grant funds were targeted to the neediest communities, Goodridge would have received assistance before now. Communities like Goodridge will suffer ill health before they can afford the new "market rate" interest FmHA is currently requiring.

LITTLE RIVER RURAL WATER ASSOCIATION, IOWA

The Little River Watershed area is a source area within the Southern Iowa Rural Water Association. It is comprised of the majority of Decatur County (except that served by the Rathbun system), the extreme southern edge of Clark County and the extreme western edge of Rindhold County. The area, excluding the towns of Leon and Lamoni, has approximately 6,100 residents and 3,496 households.

Approximately 800 of these households are economically disadvantaged. The area residents are supporting efforts to obtain a rural water system because of inadequate and poor quality water.

The shortage of potable water has become the most critical in the small towns, where improper wastewater disposal, among other factors, has caused pollution of the water supplies. In rural areas, agricultural runoff, improper abandonment of wells and feedlot runoff have caused ground water contamination which has affected what was already a poor quality of water.

A study conducted by the Iowa State University determined the only feasible source of water to be surface impoundment.

The Midwest Assistance Program has assisted the Little River Project with securing preliminary engineering and much coordination has taken place between the agencies involved. Throughout the development of the project in planned phases, there has been concern that the final user costs might become excessive, and therefore, unfeasible.

The watershed impoundment portion of the project is moving ahead.

However, with the recent budget reductions and the increased interest rates on FmHA loans, there are new concerns that the project may never be completed at user rates that people can afford.

All planning computations were made on a 5 percent FmHA interest rate. If the interest rate is 11 or 12 percent, the project is no longer feasible.

With the budget cutbacks, the timeline for construction is also extended, and the potential for higher than anticipated construction costs becomes an additional concern.

The rural communities and farm residences within the Little River Water Project are facing severe water problems, but the outlook for solving these problems has been significantly jeopardized by the increased interest rates and the reduced funding for rural development programs such as the Farmers Home Administration's Water and Waste Loan and Grant Programs.

FOREST RIVER, N. DAK.

This small eastern North Dakota town is expecting to match a Farmers Home Administration loan with an EPA grant to construct a community sewer system.

But, their calculations were based on the anticipation of a low-interest loan from FmHA. The community now finds itself in a dilemma, because with current FmHA interest rates, the many elderly and low income families will not be able to afford the user fees that will be necessary to repay the loan and provide for operation and maintenance costs.

ARGYLE, IOWA

This southeastern Iowa community of one hundred and sixty (160) residents is an example of how the current Farmers Home Administration's Water and Waste Loan and Grant Programs are now working.

This unincorporated community has failing septic systems and shallow wells with signs of contamination.

The Southeast Iowa Community Action Agency in Burlington, Iowa, armed with training and technical assistance from the Midwest Assistance Program, helped this community through the development process.

Needs assessments were done, public hearings held, comm. nity fund raising events scheduled and preliminary studies completed. The community has incorporated and established as their first priority the solving of their water problem.

In March, approximately one year after MAP's first involvement with Argyle, they received a letter of conditions from FmHA which provides for the funding of the water system. This sounds like a phenomenal success—and to this community, it is. But, to those of us who work with the FmHA programs and with many rural communities needing this assistance, we are less than overjoyed!

Argyle is getting an $82,400 loan at 11.375-percent interest and a grant of $157,600. That is approximately a 70-percent grant. In effect, grant money is being used in Argyle to offset the difference from 5-percent interest to the market rate

interest. This effectively reduces the availability of grant assistance so desperately needed in other communities throughout the state of Iowa and across the nation.

Argyle's minimum monthly user fee for 2,000 gallons of water will be $15.00. With this same monthly fee Argyle could have afforded a 5-percent interest loan of approximately twice that offered them and the FmHA could have reduced the grant to less than $80,000, saving $80,000 in grant funds for other needy communities.

Small rural communities have difficulty qualifying for EPA funding for their wastewater systems. But, when they do, in many instances, they have no alternative but to finance the 25 percent local share with a FmHA loan. Sewer rates in these communities are hardly affordable at the 5-percent interest rate. With 12 percent interest on FmHA loans, the low income communities are unable to afford the loan they need to match the EPA funds.

ARVILLA, N. DAK.

This rural North Dakota community lies on the eastern edge of the state. Many of its residents are elderly and on fixed incomes. Their septic systems are failing and this is polluting the high ground water. The community has completed a Step 1, EPA funded plan, and hopes to construct a small sewer system which will alleviate their problem.

However, the acting Mayor has indicated that if the community has to finance the local share of the project with an 11- or 12-percent interest loan, the elderly and low-income residents won't be able to afford the sewer bills.

This community may find itself rejecting EPA funds for the construction of their sewer system because FmHA interest rates are beyond the community's ability to pay.

Without some assistance that reduces the interest rates substantially below the market rate, communities such as Arvilla will do without adequate water and waste disposal facilities to the detriment of their health and the nation's well-being.

Elderly people are more readily susceptible to the effects of poor water quality than many of us. They can end up being prematurely hospitalized and institutionalized. This is an expensive alternative to the provision of safe water supplies and sanitary waste disposal.

Suitable technical assistance targeted to the small, rural community is universally recognized as an appropriate function to help these rural Americans solve complex problems. Those areas where the solutions have been easy are, generally speaking, solved. But, even some of these areas, where water quality or availability have not been a problem, are now experiencing water contamination and/or depletion of ground water supplies.

Survey returns from fifteen (15) rural legislators from the states of Iowa, Kansas, Minnesota and Missouri confirm that rural communities face difficulties in solving their water and wastewater problems. A one-page summary of the survey results is attached. (Exhibit A)

It reveals that twelve (12) of the fifteen (15) legislators were aware of rural communities in their districts who have sought unsuccessfully for federal assistance for their water/wastewater problems and the same number of respondents recognized the inability of these communities to hire the full-time consultants needed to make them competitive.

The task of bringing potable water and sanitary wastewater disposal to rural America is not completed. And, I encourage the members of this committee to consider the amendments to the Farmers Home Administration Water and Waste Loan and Grant Programs as a modest step in helping rural communities to find acceptable solutions to their water and waste disposal problems, because these amendments will help to make these programs more responsive to those rural communities in greatest need.

EXHIBIT A

SUMMARY OF RETURNS OF A WATER/WASTEWATER SURVEY SENT TO STATE LEGISLATORS FROM IOWA, KANSAS, MINNESOTA, AND MISSOURI

Returns of a water/wastewater survey from 15 rural legislators from Iowa, Kansas, Minnesota and Missouri indicate that there are indeed problems in small, rural communities with water and/or wastewater facilities.

(1) Twelve of the legislators stated that there were small, rural communities in their areas or districts with water or wastewater problems who have, in the last five years, been unsuccessful in accessing federal funds to help solve their problems.

(2) Nine of them responded positively to having communities in their areas who are in need of better operation and maintenance of their water or wastewater systems, possibly through operator training.

(3) Four indicated there were rural communities in their areas who are in violation of their National Pollutant Discharge Elimination System permits.

(4) Seven responded as having communities in their district who were having difficulty in organizing and surveying to ascertain their community's needs.

(5) Nine legislators pointed out that some of their constituents in small rural communities had raised either clean water or safe sanitary waste disposal as being a problem, either individually or in their town.

(6) Four were aware of elderly or low-income persons who had been unable to tap-in or hook-up to new water or wastewater systems in small communities because of the financial burden.

(7) Twelve indicated they knew of small communities who could not afford to hire a full-time consultant, but who needed some guidance and assistance in solving water and/or wastewater problems in their town.

(8) There were five who responded as being aware of communities who are considering alternative wastewater treatment technologies and finding it difficult.

(9) Six indicated there were rural areas in their districts who are thinking about forming a rural water district; and

(10) Four of them also pointed out that they did not feel there was adequate technical assistance available to these rural water districts to assist them in the development of their project.

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NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION,
*Washington, D.C., March 1, 1982.*

Senator JESSE A. HELMS,
*Chairman, Senate Committee on Agriculture, Nutrition, and Forestry, Dirksen Senate Office Building, Washington, D.C.*

DEAR MR. CHAIRMAN: On behalf of the National Rural Electric Cooperative Association, I would like to recommend that the rural development programs of Farmers Home Administration, along with its farm loan programs, be reauthorized under the Consolidated Farm and Rural Development Act. In respect to the rural development programs, we would point that there is a very great need for water and sewer and other kinds of community facilities in rural areas, as well as a very critical need for capital for job-creating small businesses.

When Public Law 96-438 was passed in October 1980, it provided generous authority for these programs, including $1 billion for insured water and sewer facility loans, $1.5 billion for industrial development loans, of which all but $1.4-billion were to be guaranteed, and $500-million for insured community facility loans.

While these loan levels are still realistic in view of the needs for these kinds of facilities and job-creating opportunities in rural America, it is unlikely that they will be supported by the Administration. With that in mind, we would suggest that as a minimum the loan levels and the grant levels of 1981 be approved. We would also recommend that these 1981 FmHA loan and grant levels be recommended by your Committee to the Senate Budget Committee for the fiscal 1983 budget.

In regard to the FmHA business and industrial loans, we are aware that they have come under some criticism. Undoubtedly some questionable loans have been made, but this doesn't seem to us sufficient reason to abandon the program, as the Administration is proposing.

The B&I Program was authorized by Congress in the Rural Development Act of 1972, and was perhaps the single most important provision of that legislation. Up until then, rural businesses had little chance of getting loans from SBA or EDA. Nor were rural banks in a position to tie up their capital for long periods, or make loans that involved high risks. That is one reason why the Congress gave FmHA the authority to guarantee the banks against loss.

The main purpose of the program, which FmHA has fulfilled impressively so far, was to create new job opportunities for farm and rural people so they would not be forced to move to urban areas. Rural outmigration was then a serious domestic problem. It could become a serious domestic problem again if something isn't done to counter increasing unemployment and underemployment. The B&I Program has contributed significantly to expanding jobs in rural America and, as a result, has helped to halt the rural-to-urban migration which threatened to make wastelands out of much of rural America. Farmers as well as other rural residents have benefited since over 50 percent of farm families rely on non-farm jobs for over 50 percent of their income.

If the B&I Program were eliminated, then a very serious blow will have been dealt to rural development and rural America. Past experience indicates that SBA and other urban-oriented agencies will not be able to fill the gap. In addition, the Administration is about to do away with the Economic Development Administration, which provided some of this assistance in certain rural counties. On the other hand, the B&I Program can provide assistance in all counties. There would have been no need for Congress to establish the B&I Program had these other programs been adequately serving rural areas. It would indeed be ironic during this period of increasing unemployment in rural areas if the most effective federal program for creating and safe-guarding jobs were abolished.

We appreciate this opportunity to express our views on the legislation before your Committee. If there is any additional information that we might be able to supply, please let us know.

Sincerely,

WILLIAM E. MURRAY,
*Legislative Specialist for Rural Development.*

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INDEPENDENT BANKERS ASSOCIATION OF AMERICA,
*Washington, D.C., February 12, 1982.*

Hon. WALTER D. HUDDLESTON,
*Ranking Minority Member, Committee on Agriculture, Nutrition, and Forestry, U.S. Senate, Dirksen Senate Office Building, Washington, D.C.*

DEAR SENATOR HUDDLESTON: The decisions which the Committee on Agriculture, Nutrition, and Forestry and Congress will make in the weeks ahead on the rural business and industry B & I loan guarantee program of the Farmers Home Administration will be crucial to the continued viability of that program. On behalf of the Independent Bankers Association of America, which represents almost 7,300 community banks a large portion of which are located in rural areas and smaller communities, I urge you to support the B & I loan guarantee program at levels sufficient to enable its continued successful operation on a nationwide basis.

Specifically, we ask that you: (1) recommend to the Senate Committee on Budget that $1 billion of authority for B & I be carried in the budget resolutions and related measures for fiscal year 1983 and for each subsequent year; (2) reauthorize the funding of FmHA rural business and industry loan guarantees at $1 billion for each of the 3 fiscal years beginning October 1, 1982; and (3) support the program at the above levels during the appropriations process and during administrative implementation.

A $1 billion annual loan commitment level would represent a substantial cut in the $1.5 billion ceiling for each of fiscal years 1980–1982 which was contained in P.L. 96–438, and is also less than the actual obligation levels for the program in fiscal years 1979 and 1980. A $1 billion annual authorization represents, in our judgment, the minimum level which will enable maintenance of the infrastructure which is necessary for effective operation of the program nationwide. For instance, commercial banks and secondary marketing institutions must maintain staff capability for processing and servicing of the loans. A $1 billion annual commitment level, with a measure of year-to-year continuity provided by the 3-year funding authorization, will provide a minimal basis for staff planning and other management practices within financial institutions and USDA.

The fact that demand for credit under the B & I program has been relatively slack in recent months is no justification for reducing the authorized funding below levels adequate for efficient operation. High interest rates and the economic recession have made business firms reluctant to borrow for longer-term investments in rural areas, and ambiguity regarding the actual availability of B & I funds has also contributed to soft demand. However, it is impossible to predict the timing of an economic turnaround so that Congress could authorize additional funding once economic recovery is underway—especially in order for business financing under B & I to contribute to sustaining the recovery on the front end.

When the B & I program is judged in terms of Congressional intent expressed in the Rural Development Act of 1972 and subsequent amendments—which was to encourage productive economic activity and employment by the private sector in rural areas, this loan guarantee program has been quite successful. Since its inception, 3,551 borrowers have participated; $3,546,000,000 in loans have been closed; and $41 million of losses to the government (or 1.15 percent of the value of loans closed) have been incurred. The 1 percent guarantee fee assessed by FmHA has yielded a total of $31.2 million, so that 76 percent of the losses have been offset by proceeds

from the guarantee fee. In view of this offset, and the fact that these loan guarantee commitments are not carried in the regular budget, the additional economic activity and employment in rural communities resulting from this program have been achieved with virtually no direct impact on budget outlays and deficits.

The relatively low loss ratio associated with B & I loans is partly attributable to the fact that the loans were initiated essentially by local community banks upon which the FmHA relies heavily for evaluation of loan applications and servicing of loans after closing. Participation by a local independent bank in the B & I program can contribute significantly to the bank's liquidity and capacity to serve borrowers, in two ways: (1) the guaranteed portion of a B & I loan is readily salable in secondary markets; and (2) the guaranteed portion of the loan does not apply against the individual legal lending limit of the bank and therefore the bank is able to make larger loans to individual borrowers when a guarantee is affixed.

For these reasons related to bank liquidity, and for other reasons, operation of the B & I loan guarantee program should not reduce the credit available to farmers from government and private sources. Since the loan guarantee commitments are off budget, the provision of funding to B & I does not involve a tradeoff with other farm income and credit programs administered by USDA. Furthermore, the handling of B & I guaranteed loans by independent banks is useful in maintaining the banks' general competitiveness and their capacity to serve farm and ranch borrowers within their local service areas.

The B & I loan guarantee program has no adverse "crowding out" effect in the credit markets, since this program guarantees private sector loans in which government involvement is only residual, based upon the guarantee. Although the program intentionally results in net new credit extended to business and industrial enterprises in rural areas, this is fully justifiable as a counterbalance to the fact that private credit markets tend to overestimate the risk of investments in rural areas.

In summary, the IBAA recommends firm reauthorization of the rural business and industry loan guarantee program at a $1 billion annual level for new guarantee commitments, including multi-year authorizations to provide the continuity which is necessary for successful program management.

We look forward to supporting you wherever possible in achieving this objective.

Sincerely,

W. C. BENNETT, *President.*

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ENVIRONMENTAL POLICY CENTER,
*Washington, D.C., April 30, 1982.*

Hon. PAULA HAWKINS,
*Chairman, Subcommittee on Agricultural Credit and Rural Electrification, Senate Committee on Agriculture, Nutrition, and Forestry, Russell Senate Office Building, Washington, D.C.*

DEAR SENATOR HAWKINS: This statement, and attachments, are submitted to the hearing record of April 21, 1982 concerning S.2314 and reauthorization of funding levels for FmHA loan programs. We ask that this statement and its attachments be included in the printed hearing record.

The Environmental Policy Center (EPC) wishes to go on record opposing any legislation aimed at reducing the amount of federal credit available to the nations' farmers. Moreover, EPC favor the immediate release of the $600 million in Economic Emergency funds authorized in the 1981 farm bill, and supports and immediate morantorium on all FmHA foreclosure actions on outstanding farm loans.

The Environmental Policy Center finds an increasing amount of evidence—based on reports from all over the country as well as USDA data—that at least 200,000 and possibly as many as 600,000 of the nation's 2.4 million farmers are in serious financial trouble, and that many of these farmers are facing one or more of the following situations: 1) they are in danger of losing their entire farm by the end of 1982 or 1983; 2) they are currently, or will be shortly, forced to sell off equity in their farming operations in order to reduce indebtedness, cover costs, and generally compensate for low farm prices; and/or 3) they are having to restructure debt repayment schedules and some are using farm-based assets and equity to cover operating costs. (See attachments).

The Environmental Policy Center fears that a reduction in the nation's farms and farmers during this time of economic difficulty will have far-reaching consequences for the nation's agricultural resource base and control of food production. As fewer farmers are left to make the conservation improvements that a well-tended food

producing resource base needs to remain viable, agricultural land, soil and water resources will be damaged.

Farm reduction also means further farm consolidations, and a future of largescale agriculture—an agriculture more reliant on heavy inputs of chemcials, energy and capital; and agriculture that is harder on the resource base, and one that may be of questionable economic efficiency over the longer term.

By allowing the current economic situation to undermine family farm agriculture, we will be setting the stage for larger and larger farms that are even more heavily indebted, highly specialized in one or two agricultural commodities, and vulnerable to swings in the marketplace. Allowing this, we will also be setting the stage for a kind of farming that mines the landscape to service debt and meet financial scales of efficiency rather than biological ones. And on that path, we are surely courting disaster.

Unlike other consumer and business borrowers, farmers are bound by the seasons and cycle of planting, and cannot wait for interest rates to go down, or defer decisions to plant or harvest. For many farmers, they have no alternative but to borrow, regardless or interest rates. Delay can mean the difference between success or failure. Therefore, farmers are in something of a special category when it comes to credit. The farm sector's credit burden would not be so overbearing if farmers received their full cost of production. And while some are suggesting that price support programs be cut still further, with farm incomes falling to Depression-era lows, this is not the time to be undermining farm programs. Although it is true that a number of farmers who are now in financial difficulty with high debt-to-equity ratios borrowed heavily on rising land values and were speculating on the future—farmers alone are not entirely responsible for this situation. The federal government and the commercial farm credit institutions are at least partially responsible for this situation since they encouraged many farmers to borrow and expand during the 1970s.

### THE FARM ECONOMY AND AGRICULTURAL RESOURCES

In its 1982 Survey of Rural and Economic Conditions, the North Dakota Farmers Union finds that 50 percent of the Soil Conservation Offices responding to its survey report that soil conservation activities have decreased in their areas. However, 76 percent of these offices indicate that there is an increase in soil erosion in their areas. This North Dakota survey also reports that "large block cropland is increasing" throughout the state, and that "as costs for farmers go up and commodity prices remain low, the temptation to produce more increases even at the risk of land damage".

### "DOMINO EFFECT" OF U.S. FARM CRISIS

Over the last 20 years or so, American agriculture has enjoyed a very healthy assets picture, built largely on the rising value of farmland. However, some bankers, government officials and farm organizations have expressed fears that as the farm economy becomes more depressed, the value of farmland may begin to slide, thus creating a "domino effect" or chain reaction, throughout all parts of the rural economy, as farm-related businesses and workers are all impacted by the lack of farm spending and farm income. The North Dakota Farmers Union has described such a chain reaction as follows:

"As credit limits are overrun, owner equity diminishes, land values and machinery worth diminish. The downward slide picks up momentum that impinges on the local tax base, affects the purchasing power of farmers first and then businessmen, not only on North Dakota's main street, but of the laid-off workers in farm machinery plants, steel plants, rubber plants and the whole interrelated distribution chain."

But perhaps the most serious effect of such a slide in agricultural assets and the agricultural economy, is that the price and value of farmland will be temporarily depressed, allowing a few well-positioned landholders, credit institutions and investors to acquire farmland more cheaply than they could during normal economic conditions.

### SHIFT IN FARM ASSETS

As the current economic situation continues to take a toll of farms and farmers throughout rural America, some shift in assets from the farm sector to the non-farm sector will also occur, possibly increasing the overall debt-to-asset ratio in the farm

sector as a whole, undermining the credit worthiness of all farmers, and particularly that of low-equity and beginning farmers.

As foreclosures, bankruptcies, and farm sales mount, banks, insurance companies and other credit-related institutions will acquire farm assets and farmland to cover outstanding debt. Depending on the severity of the situation, the shift in potential assets to the non-farm sector could be quite substantial.

According to the Federal Reserve Bank of Kansas, for example, life insurance companies already hold more farm real estate debt than FmHA.

Moreover, independent of their farm credit holdings, life insurance companies are acquiring large tracts of farmland throughout the U.S. as both a long-term investment, and as a way to profit from favorable tax treatment under investment tax credit and depreciation allowances. In Nebraska, for example, Prudential Insurance Company, through a subsidiary called PG Realty, recently acquired at least 35,000 acres of farmland in three counties. Other insurance companies have purchased farmland in Arkansas, Illinois, and Mississippi. Insurance companies and insurance-company administered pension funds have supported farmland investment schemes in 1977 and 1980, and continue to eye prime farmland and agricultural operations in the Midwest and other regions of the country for investment purposes.

### THE ROLE OF THE EXPORT MARKET

The rising value of U.S. farmland, and attractiveness of American agriculture as an investment over the past 10 years or so, seems to be tied—at least in part—to the world food market and the prospect of farm export expansion.

For example, USDA noted in a 1981 study, "A Time To Choose":

"In current dollars, physical assets of farm operations (land and buildings, machinery, livestock, and crops stored on and off farms) more than tripled in value between 1960 and 1978, with the major increases occurring after 1972's boom in grain prices, (i.e. following the large Russian grain deals). . . . In the seven year period of 1972 to 1978, the value of U.S. farm assets more than doubled. This increase of more than $400 billion was nearly three times the total farm earnings in the same period and equivalent to total farm income for the previous 38 years."

However, one of the economic difficulties presently facing American agriculture is slack export demand. Yet, the current Administration believes that the nation's agricultural problems will be solved by a booming export market. But, might continuing U.S. reliance on the export market increasingly put American agriculture on a cyclical "boom and bust" economic footing, with increasing indebtedness and speculation occurring with each "boom" period, and more foreclosures, farm bankruptcies and further farm consolidation following each "bust" period?

USDA's report, "A Time To Choose," found that instability in agriculture "significantly increased in the 1970's with the advent of rapid growth in foreign markets". USDA's report also noted that those farms most reliant on farm income and debt financing would be most vulnerable to changes in farm exports.

### NONPRODUCTIVE FARM BORROWING

Much of the farm borrowing in the U.S. is used to underwrite the consolidation of farms and farmland. According to USDA, farm sector debt may rise to $600 billion by 1990. Farms with annual sales of $100,000 or more will account for about one-half of this farm debt. However, what is troubling about this borrowing pattern is that roughly one-half of all borrowed funds during the 1980–1990 period will be used to finance transfers of farmland, and so will add little to the productive capacity of the farm sector. And most of these land transfers will be to larger farms.

### OWNERSHIP, CONTROL AND ROLE OF USDA

Further farm consolidation will mean further economic concentration in production agriculture. Already in the U.S., 6 percent of all farms account for 54 percent of all farmland; 3 percent of all farms produce 40 percent of all farm products. A mere 3 percent of all U.S. households own any farmland whatsoever. The nation is rapidly approaching an aristocratic profile of agricultural landownership that our founding forefathers sought to avoid, and our historical record of public land disposal and agricultural settlement policies would seem to belie.

The nation's agricultural land acts, and its farm programs in particular, have sought to keep people on the land for reasons of political stability as well as economic opportunity.

Our understanding of the historical charter of the FmHA is one molded, in part, by that historical past; of keeping people on the land—a policy designed to assist

farmers and keep them in business, not to ask them to quit farming as FmHA has done recently in North Dakota, or to accelerate loan payment schedules, as FmHA has done in Texas.

Unless USDA and FmHA can move to assure the nation's farmers in this time of economic difficulty, then we can only conclude that they are agents of further farm consolidation. Nor is this the time for FmHA and USDA to "stonewall" the release of economic emergency funds.

Rather, FmHA should be moving to strengthen its criteria of lending in order to assist bona fide, live-on-the-land family farming by incorporating local ownership, local residency and anti-speculative prohibitions into its lending policies. Non-farm corporations and absentee investors should be strictly prohibited from using FmHA programs, or any other federal credit program, for the purpose of agricultural speculation or competing with family farmers.

Within FmHA itself, budgetary savings and more efficient federal lending in the farm sector would result from a careful restructuring of federal farm credit programs designed to serve the truly credit-needy; not those operations that have achieved high equity and relative levels of economic efficiency. Moreover, FmHA could do more for local farm economies by focusing on farm lending rather than non-farm lending. USDA has noted, for example, that since 1960, an enormous change has occurred in the emphasis and direction of FmHA programs. The USDA report, A Time To Choose, has noted that in 1960, FmHA administered eight programs, of which farm-operating loans accounted for 64 percent and farm ownership loans accounted for 14 percent of total funds. In 1979, FmHA operated at least 23 programs, with farm operating loans accounting for 6 percent and farm ownership loans accounting for 5 percent of all funds.

The Environmental Policy Center finds it patently unfair to rationalize balancing the federal budget and reducing federal deficits on the backs of farmers who need credit help, while other programs and subsidies remain unscathed. Moreover, it is more than unfair that while the Reagan Administration tries to make a saving in the FmHA area that penalizes some of the nation's most needy farmers, it has agreed to extend a more-than-generous package of federal subsidies to some of the nation's wealthiest farmers—mostly in California—in the current "reform" of the 1902 Reclamation Act.

Further, U.S. Rural Electrification "generating and transmission" co-ops are hurting all farmers by their huge loan guarantee demands in the U.S. credit market—money which is used in part to help build investor-owned power plants. Rural electric co-ops could help all farmers—and reduce federal borrowing—by working to advance energy conservation and alternative energy technologies, creating another kind of economic ripple effect that would promote jobs and new investments in rural America.

And finally, the Environmental Policy Center wishes to thank the Chairman for the opportunity to submit this statement outlining our views on the current farm credit situation and the mounting economic difficulties now facing our nation's farmers.

In summary, EPC believes that the quality of the nation's agricultural resource base, as well as the economic security of the nation's farm system, will be well served by agricultural credit policies that promote economic opportunity for beginning farmers, discourage speculation and absentee investment in agricultural land and farming operations, and generally work to keep the nation's farm system widely owned.

If we can be of further assistance to your subcommittee on this issue, please contact us.

Respectfully,

JACK DOYLE,
*Washington Representative.*

Enclosure.

REPORTS AND OBSERVATIONS CONCERNING THE CURRENT ECONOMIC CONDITION OF THE NATION'S FARM SYSTEM

THE GENERAL FARM SITUATION

According to one report in the Journal of Commerce, "about 120,000 of the nation's 2.4 million farmers are in serious financial trouble and could lose their farms if the recession lingers for another year". (1)

Newsweek reports that "millions of farmers are operating at severe losses . . ." and that total farm debt is now "about 13 times as high as this year's projected (farm) income". (2)

According to one FmHA official, "if you take 1980 and 1981, it's the first time since 1933 and 1934 you've had back-to-back years in which the cost of producing on the farm was more than what the farmer got for growing it". (3)

One banker from DeWitt, Iowa, serving on the agricultural credit committee of the American Bankers Association, has noted that farmland values would collapse if thousands of farms were put up for auction. (1)

According to James Eatherly, chairman of the Agricultural Bankers Division of the American Bankers Association "net farm income may slide as low as $14 billion or $14.5 billion in 1982 . . ." In summarizing his statement before the U.S. Senate Agriculture Subcommittee on Agriculture Credit, Eatherly concluded ". . . the deteriorated financial condition of farmers is primarily due to low livestock and crop prices (and in some areas by below average yield), high interest rates, and high operating costs. This has been accompanied by a general decrease in value of inventories and capital items, resulting in a decline in net worth. We bankers . . . are very concerned about the farm economy of 1982". (4)

Farm expenses have risen from $75.9 billion in 1975 to $141.5 billion in 1981. Farm income, on the other hand, may drop from a 1975 level of $24.5 billion to a possible low of $14.5 billion in 1982. (5)

During the 1960s, interest outlays represented about 16 percent of net farm income; today, total interest outlays equal farm income. (5)

According to U.S. Secretary of Agriculture John Block, "total farm debt has doubled in the last five years and farmers' debt servicing burden has become a major problem". (6)

A University of Wisconsin study reported in 1979 that the average financial obligation of 165 low-equity operations exceeded income by nearly $11,000. Other economists at the University of Wisconsin have recently indicated that low-equity farmers (those who are just beginning farming who haven't had time to build up equity to withstand harder times) may have to repay as much as $2.37 in debt for every $1.00 earned in the sale of farm products. (5)

According to the president of the First National Bank and Trust Company of Columbia, Missouri: "The only people farming now want to farm. They love to farm. There's not much economic incentive in it anymore". (3)

### FARM FORECLOSURES, BANKRUPTCIES, AND DELINQUENCY RATES

More than half of the nation's farmers—about 1.2 million—have borrowed money from FmHA, accounting for about 11 percent of the nation's $200 billion farm debt. Some 218,000 FmHA farm loans are in technical default. (6)

According to Time, "While the FmHA has begun foreclosure proceedings against only 2,500 farmers so far, many more are either quitting the fields or selling parts of their acreage to stay in business." (7)

According to one agricultural economist, "for every one (farmer) being foreclosed, there probably are 10 who are on the brink . . . There are literally thousands who cannot survive another low-income year . . . (If I) were to guess, I'd say that a fourth of all farmers (roughly 600,000) are in trouble, are on a fairly thin edge financially . . ." (3)

The National Farmers Union reports from U.S. Farmers Home Administration documents dated March 3, 1981, that 35 percent of all FmHA farm borrowers are delinquent in their loan payments, accounting for more than 100,000 delinquencies nationwide. (5)

More than 9,500 FmHA farm borrowers in Georgia who have missed loan payments are now classified as "delinquent" borrowers. (8)

Farm Credit System Governor, Donald Wilkinson, has stated USDA would weaken all farmers' financial posture if the FmHA started widescale foreclosures. (1)

According to the vice president of Olney Trust and Banking Company in Olney, Illinois, 20 percent to 30 percent of all farm operating loans are being restructured and extended by securing the debt with land rather than crops. (9)

One attorney in Columbia, Missouri, who handles bankruptcies says that he has noticed "a tremendous increase in the number of farmers" who come to see him. (3)

One farmer from Salem, Illinois, quoted in the Wall Street Journal, explains: "If we don't have a real good year, there are going to be a lot more farmers (going) bankrupt. Around here, there are just lots of (farm) sales, and I mean lots of them. And its younger farmers, guys like me (who are going out of business)." (10)

The vice president of Iowa State Bank noted recently, "in the Des Moines Register last Sunday there were 31 farms sales. Normally when we get into this time of year, the farm sales are over." (10)

According to one report in the Journal of Commerce, government-forced foreclosures would have a "ripple effect" on other farm lending institutions and would weaken the ability of farmers to secure loans because the value of their land and equipment would decline. (1)

The chairman of the American Bankers Association agriculture committee has stated: "I don't think there will be a flood of bankruptcies in 1982, but there will be a surge in 'encouraged' (farm) sales". (11)

HOW THE BANKERS SEE IT

A survey of 350 commercial banks by the American Banking Association has reported "an alarming deterioration in the overall financial condition" of their farm borrowers. (12)

According to a North Dakota Farmers Union survey of 102 banks and farm credit institutions in North Dakota, 90 percent say that farm loan repayment by their farm borrowers ranges from "very difficult" to "out of the question", due to the widening gap between farm prices and farm production costs. The survey also revealed that 23 percent of these lending agencies were experiencing delinquency rates ranging from 10 to 45 percent. A few reported delinquency rates as high as 85 percent.

One banker in Fairbury, Illinois, notes: "I'd say 5 percent of Midwest farmers may have trouble surviving the year. And an additional 15 percent may not get through the next year". (7)

A representative for the State Bank of Alcester, South Dakota, reports that 20 to 30 percent of their farm borrowers "are in trouble", and that "it is almost impossible" to construct a positive cash flow statement for farmers who have any appreciable amount of debt. (5)

In Colorado, production credit associations, co-ops and the Federal Land Bank are telling farm organizations that half of their farm borrowers could be in trouble by the Fall, and might not be able to continue farming. (3)

The vice president of Moultrie National Bank in Colquitt County, Georgia, says, "we've just about stopped making short-term operating loans . . . because there's little chance the average farmer could pay them back from this year's crops".

Donald Wilkinson, Governor of the Farm Credit System, has stated that cooperative lending institutions are denying credit this spring to farmers they supported a year ago. (1)

The president of Idalou State Bank in Idalou, Texas, reports that "third and fourth generation farmers, good farmers", are losing money because of the growing gap between income and expenses. (5)

The president of Farmers State Bank in Hart, Texas, reports that irrigated corn and cotton farmers with good yields (i.e., 180 bu./acre corn and 2-bale/acre cotton) cannot pay back their debt. (5)

The American Bank of Commerce in Wolffort, Texas, reports that 75 to 80 percent of its farm borrowers are in "very bad shape", and that if prices don't improve, 30 to 35 percent of the farmers in that area will not be farming again in 1983. (5)

SOURCES

(1) Lee Egerstrom, "Federal Units Urged To Support Farmers", Journal of Commerce, April 29, 1982.

(2) "A Harvest of Despair", Newsweek, April 12, 1982.

(3) Gregory Jaynes, "U.S. Farmers Said to Face Worst Year Since 1930's", New York Times, March 28, 1982.

(4) Testimony of James R. Eatherly, on behalf of the American Bankers Association, before the U.S. Senate Subcommittee on Agricultural Credit and Rural Electrification, Senate Committee on Agriculture, Nutrition and Forestry, April 21, 1982.

(5) Statement of Paul R. Sacia, Legislative Assistant, National Farmers Union, Presented to the Subcommittee on Agricultural Credit and Rural Electrification, U.S. Senate Committee on Agriculture, Nutrition and Forestry, concerning reauthorization of FmHA, Washington, D.C., April 21, 1982.

(6) Seth S. King, "Secretary Resists Bid to Use Emergency Farm Fund", New York Times, April 18, 1982.

(7) "Hard Times in the Heartland", Time, April 12, 1982.

(8) Seth S. King, "Debt Has Outgrown Crops in Georgia", New York Times, April 4, 1982.

(9) Michael Rosenbaum, "Bankers Refinancing Farmers' Operating Debt", Journal of Commerce, April 21, 1982.
(10) Claudia Waterloo, "As Planting Season Begins, Farmers Look For New Ways to Cut Costs—and Survive", Wall Street Journal, April 28, 1982.
(11) Marcia Zarley Taylor, "Blue Chip Farm Credit Turns Anemic", Farm Journal, January 1982.
(12) "Bank Survey Shows Ag Economy Concern", East River Guardian (SD), April 1982.
(13) Survey of Rural and Economic Conditions, 1982, North Dakota Farmers Union, April 1982.

II

97TH CONGRESS
2D SESSION

# S. 2314

To amend the Consolidated Farm and Rural Development Act.

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IN THE SENATE OF THE UNITED STATES

MARCH 30 (legislative day, FEBRUARY 22), 1982

Mrs. HAWKINS (by request) introduced the following bill; which was read twice and referred to the Committee on Agriculture, Nutrition, and Forestry

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# A BILL

To amend the Consolidated Farm and Rural Development Act.

*Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,* That, effective October 1, 1982, the Consolidated Farm and Rural Development Act is amended—

(1) in section 307(a)(3) by deleting the designation "(A)" after "(3)" and by deleting subparagraph (B);

(2) in section 307(a)(6)(B) by deleting clause (viii) and inserting in lieu thereof "(viii) clause (5) of section 312(a).";

(3) by deleting section 310D;

(4) in section 316(a) by deleting "(1)" after "(a)", by deleting in the second sentence "and loans as pro-

vided in paragraphs (2) and (3)" after "except for guaranteed loans", and by deleting paragraphs (2) and (3);

(5) in section 333(c) by deleting "(or, in the case of a borrower under section 310D of this title, the borrower may be able to obtain a loan under section 302 of this title)"; and

(6) in section 346 by deleting subsection (d) and amending subsection (b) to read:

"(b)(1) To the extent and in such amounts as are approved, in advance, in appropriation Acts, loans for each of the fiscal years 1983, 1984, and 1985 are authorized to be insured, or made to be sold and insured, or guaranteed under the Agricultural Credit Insurance Fund as follows:

"(A) real estate loans, $818,000,000, including $775,000,000 for farm ownership loans of which $700,000,000 may be for insured loans and $75,000,000 may be for guaranteed loans with authority to transfer 25 per centum of such amounts between categories, and $31,000,000 for water development, use, and conservation loans of which $25,000,000 may be for insured loans and $6,000,000 may be for guaranteed loans with authority to transfer 25 per centum of such amounts between categories;

"(B) operating loans, $1,510,000,000 of which $1,460,000,000 may be for insured loans and

$50,000,000 may be for guaranteed loans with authority to transfer 25 per centum of such amounts between categories; and

"(C) emergency loans, not to exceed $1,540,000,000.

"(2) To the extent and in such amounts as are approved, in advance, in appropriation Acts, loans for each of the fiscal years 1983, 1984, and 1985 are authorized to be insured, or made to be sold and insured, under the Rural Development Insurance Fund as follows:

"(A) water and waste disposal loans, $300,000,000; and

"(B) community facility loans, $130,000,000.".

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